NATIONAL CREDIT UNION ADMINISTRATION

RULES AND REGULATIONS

TRANSMITTAL SHEET CHANGE 2

NCUA 8006 (M3500) DATE: February 1999

TO: THE BOARD OF DIRECTORS OF THE FEDERAL CREDIT UNION OR THE FEDERALLY INSURED CREDIT UNION ADDRESSED:

This is Change 2 to the National Credit Union Administration Rules and Regulations (Revised August 1998)

1. **PURPOSE.** To update the National Credit Union Administration Rules and Regulations (Revised August 1998) in the following manner:

a. **Section 701.1—Federal credit union chartering, field of membership modifications, and conversions.** Revised paragraph.

b. **Section 701.21—Loans to Members and Lines of Credit to Members.** Revised paragraph (c)(7)(ii)(C); added new paragraph (g)(7).

c. **Section 701.23—Purchase, Sale, and Pledge of Eligible Obligations.** New sentence added to the end of paragraph (b)(1)(iv) and revised paragraph (b)(3).

d. **Section 707.4—Account disclosures.** New sentence added to the end of paragraph (b)(6)(iii).

e. **Section 707.5—Subsequent disclosures.** Amended by removing paragraph (c) and redesignating paragraph (d) as new paragraph (c).

f. **Section 707.8—Advertising.** New paragraph (c)(6)(iii) added and revised paragraph (e)(2)(i).

g. **Section 707.9—Enforcement and record retention.** Revised paragraph (b).

h. **Appendix A to Part 707.—Annual Percentage Yield Calculations.** Revised third sentence in the introductory text to Part I; revised the first sentence of the introductory text to Part I.A. General Rules; and added a new section E to Part I.

i. **Appendix B to Part 707—Model Clauses and Sample Forms.** Added new paragraph (i)(v) under B–1 Model Clauses for Account Disclosures.

j. **Appendix C to Part 707—Official Staff Interpretations.** Removed paragraph (c)1 under Section 707.5 and redesignated (d)1 as new paragraph (c)1; removed paragraph (e)(2)(i)2 under Section 707.8

k. **Part 708a—Conversion of Insured Credit Unions to Mutual Savings Banks.** Revised entire part.

2. **INSTRUCTIONS:**

a. Your August 1998 NCUA Rules and Regulations should be updated as follows:

REMOVE OLD PAGES	INSERT NEW PAGES
i–xii	i–xii
701–1 thru 701–26	701–1 thru 701–26
707–3 thru 707–56	707–3 thru 707–56
708a–1 thru 708a–4	708a–1 thru 708a–2

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Part 701

Organization and Operations of Federal Credit Unions

§ 701.1 Federal credit union chartering, field of membership modifications, and conversions.

National Credit Union Administration policies concerning chartering, field of membership modifications, and conversions are set forth in Interpretive Ruling and Policy Statement 99–1, Chartering and Field of Membership Policy. Copies may be obtained by contacting NCUA at the address found in § 790.2 of this chapter. The IRPS is incorporated into this section.

§ 701.2 Incorporation by reference.

(a) The publication used by Federal credit unions, which is identified in this chapter, is hereby incorporated by reference pursuant to 5 U.S.C. § 552(a)(1) and the regulation issued thereunder.

(b) Copies of the publication prescribed in this chapter may be obtained on request addressed to National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

(c) Revisions or amendments of the publication may be issued from time to time by the National Credit Union Administration. A historic file of such amendments or revisions is maintained and made available for inspection at the National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

(d) The publication listed below is hereby incorporated by reference:

(1) Federal Credit Union Bylaws. (Approved by the Office of the Federal Register through June 30, 1982.)

(e) Copies of this publication are on file with the Director, Office of Federal Register, National Archives and Records Service, General Services Administration, Washington, D.C. 20408. The text of any changes in said publication will be filed with the Director, Office of the Federal Register, and a notice thereof will be periodically published in the Federal Register.

§§ 701.3–701.5 [Reserved]

§ 701.6 Fees paid by Federal credit unions.

(a) *Basis for assessment.* Each calendar year or as otherwise directed by the Board, each Federal credit union shall pay to the Administration for the current National Credit Union Administration fiscal year (January 1 to December 31) an operating fee in accordance with a schedule as fixed from time to time by the National Credit Union Administration Board based on the total assets of each Federal credit union as of December 31 of the preceding year or as otherwise determined pursuant to paragraph (b) of this section.

(b) *Coverage.* The operating fee shall be paid by each Federal credit union engaged in operations as of January 1 of each calendar year, except as otherwise provided by this paragraph.

(1) *New charters.* A newly chartered Federal credit union will not pay an operating fee until the year following the first full calendar year after the date chartered.

(2) *Conversions.* A state chartered credit union that converts to Federal charter will pay an operating fee in the year following the conversion. Federal credit unions converting to state charter will not receive a refund of the operating fee paid to the Administration in the year in which the conversion takes place.

(3) *Mergers.* A continuing Federal credit union that has merged with another credit union will pay an operating fee in the following year based on the combined total assets of the merged credit union and the continuing Federal credit union as of December 31 of the year in which the merger took place. For purposes of this requirement, a purchase and assumption transaction wherein the continuing Federal credit union purchases all or essentially all of the assets of another credit union shall be deemed a merger. Federal credit unions merging with other Federal or state credit unions will not receive a refund of the operating fee paid to the Administation in the year in which the merger took place.

(4) *Liquidations.* A Federal credit union placed in liquidation will not pay any operating fee after the date of liquidation.

(c) *Notification.* Each Federal credit union shall be notified at least 30 days in advance of the schedule of fees to be paid. A Federal credit union may submit written comments to the Board for consideration regarding the existing fee schedule. Any subsequent revision to the schedule shall be provided to each Federal credit union at least 15 days before payment is due.

(d) *Assessment of Administrative Fee and Interest for Delinquent Payment.* Each Federal credit union shall pay to the Administration an administrative fee, the costs of collection, and interest on any delinquent payment of its operating fee. A payment will be considered delinquent if it is postmarked later than the date stated in the notice to the credit union provided under § 701.6(c). The National Credit Union Administration may waive or abate charges or collection of interest if circumstances warrant.

(1) The administrative fee for a delinquent payment shall be an amount fixed from time to time by the National Credit Union Administration Board and based upon the administrative costs of such delinquent payments to the Administration in the preceding year.

(2) The costs of collection shall be the actual hours expended by Administration personnel multiplied by the average hourly salary and benefits costs of such personnel as determined by the National Credit Union Administration Board.

(3) The interest rate charged on any delinquent payment shall be the U.S. Department of the Treasury Tax and Loan Rate in effect on the date when the payment is due as provided in 31 U.S.C. § 3717.

(4) If a credit union makes a combined payment of its operating fee and its share insurance deposit as provided in § 741.4 of this chapter and such payment is delinquent, only one administrative fee will be charged and interest will be charged on the total combined payment.

§§ 701.7–701.11 [Reserved]

§ 701.12 Supervisory committee audits and verifications.

SECTION 701.12 BECOMES EFFECTIVE ON 12/31/96. The section as it appears in the April 1996 publication is effective until that time.

(a) *Definitions.* As used in this chapter:

(1) *Agreed-upon procedures engagement* refers to the performance by an independent, licensed certified public accountant of an engagement in which the scope is limited to applying specified agreed-upon procedures to one or more specified elements, accounts or items of a financial statement. Such procedures are insufficient to express an opinion regarding either the financial statements taken as a whole, or the specified elements, accounts or items under examination.

(2) *Compensated auditor* refers to any accounting/auditing professional, excluding credit union employees, who is compensated for performing more than one compensated supervisory committee audit and/or verification of members' accounts, or opinion audit, per calendar year.

(3) *Financial statements* refers to a presentation of financial data, including accompanying notes, derived from accounting records of the credit union, and intended to disclose a credit union's economic resources or obligations at a appoint in time, or the changes therein for a period of time, in conformity with GAAP or RAP, as defined herein. Each of the following is considered to be a financial statement: a balance sheet or statement of financial condition; statement of income or statement of operations; statement of undivided earnings; statement of cash flows; statement of changes in members' equity; statement of assets and liabilities that does not include members' equity accounts; statement of revenue and expenses; and statement of cash receipts and disbursements.

(4) *GAAP* is an acronym for "generally accepted accounting principles" which refers to the conventions, rules, and procedures which define accepted accounting practice. GAAP includes both broad general guidelines and detailed practices and procedures, provides a standard by which to measure financial statement presentations, and encompasses not only accounting principles and practices but also the methods of applying them.

(5) *GAAS* is an acronym for "generally accepted auditing standards" which refers to the standards approved and adopted by the American Institute of Certified Public Accountants which apply when an "independent, licensed certified public accountant" audits financial statements. Auditing standards differ from auditing procedures in that "procedures" address acts to be performed, whereas "standards" measure the quality of the performance of those acts and the objectives to be achieved by use of the procedures undertaken. In addition,

auditing standards address the auditor's professional qualifications as well as the judgment exercised in performing the audit and in preparing the report of the audit. Copies of GAAS may be obtained from the AICPA, Order Department, Harborside Financial Center, 201 Plaza Three, Jersey City, NJ 07311–3881, telephone (800) TO–AICPA or (800) 862–4272.

(6) *Independence* and *Independent* means the impartiality necessary for the reliability of the compensated auditor's findings. Independence requires the exercise of fairness toward credit union officials, members, creditors and others who may rely upon the supervisory committee audit report.

(7) *Internal controls* refers to the process, established by the credit union's board of directors, officers and employees, designed to provide reasonable assurance of reliable financial reporting and safeguarding of assets against unauthorized acquisition, use, or disposition. A credit union's internal control structure consists of five components: control environment; risk assessment; control activities; information and communication; and monitoring. Reliable financial reporting refers to preparation of financial statements that "present fairly" the financial position of the credit union and results of its operations and its cash flows, in conformity with GAAP or RAP, as defined herein. Internal control over safeguarding of assets against unauthorized acquisition, use, or disposition refers to prevention or timely detection of transactions involving such unauthorized access, use, or disposition of assets which could result in a loss that is material to the financial statements.

(8) *Licensed, certified public accountant* refers to an accounting/auditing professional who has received a certificate and license from a duly-appointed state licensing authority to practice accounting/auditing, and is independent as defined herein.

(9) *Opinion audit* refers to an examination of the financial statements performed by an independent, licensed, certified public accountant in accordance with GAAS. The objective of an "opinion audit" is to express an opinion as to whether those financial statements of the credit union present fairly, in all material respects, the financial position and the results of its operations and its cash flows in conformity with GAAP or RAP, as defined herein.

(10) *RAP* is an acronym for "regulatory accounting practices" which refer to the conventions, rules, and procedures governing accepted accounting practices, other than GAAP, for credit unions and having the substantial support of either the NCUA or the applicable state credit union supervisor.

(11) *Related party transactions* refers to transactions among or between parties where one party controls or can significantly influence the management or operating policies of the other so as to prevent the other party from pursuing exclusively its own interests. Examples of related parties include: executive management, board members, supervisory committee members, credit committee members, and employees, and their families. Examples of "related party transactions" include: interest-free loans or loans at below market rates; sale of real estate significantly below appraised value; nonmonetary exchange of property; below market fees, and making of loans lacking scheduled terms for repayment.

(12) *Reportable conditions* refers to a matter coming to the attention of the independent, compensated auditor which, in his or her judgment, represents a significant deficiency in the design or operation of the internal control structure of the credit union, which could adversely affect its ability to record, process, summarize, and report financial data consistent with the representations of management in the financial statements.

(13) *Specified elements, accounts or items of a financial statement* refers to accounting information that is a part of, but significantly less than, a financial statement. These may be directly identified in a financial statement or notes thereto; or they may be derived from a financial statement by analysis, aggregation, summarization, or mathematical computation.

(14) *Substantive testing* refers to testing of details and analytical procedures to detect material misstatements in the account balance, transaction class, and disclosure components of financial statements.

(15) *Supervisory committee* refers to a supervisory committee as defined in Section 111(b) of the Federal Credit Union Act, 12 U.S.C. 1761(b). For some federally-insured state chartered credit unions, the "audit committee" designated by state statute or regulation is the equivalent of a supervisory committee.

(16) *Supervisory committee audit* refers to an examination of specified elements, accounts or items of the credit union's financial statement to the full extent required in this part. An opinion audit as defined herein exceeds the

requirements of a "supervisory committee audit."

(17) *Working papers* refers to the principal record, in any form, of the work performed by the auditor and/or supervisory committee to support its findings and/or conclusions concerning significant matters. Examples include the written record of procedures applied, tests performed, information obtained, and pertinent conclusions reached in the engagement, proprietary audit programs, analyses, memoranda, letters of confirmation and representation, abstracts of credit union documents, reviewer's notes, if retained, and schedules or commentaries prepared or obtained by the independent, compensated auditor.

(b) *Supervisory committee responsibilities.* (1) The supervisory committee is responsible for ensuring that:

(i) The financial condition of the credit union is accurately and fairly presented in the credit union's financial statements; and

(ii) The credit union's management practices and procedures are sufficient to safeguard members' assets.

(2) To meet its responsibilities, the supervisory committee shall determine whether:

(i) Internal controls are established and effectively maintained to achieve the credit union's financial reporting objectives which must be sufficient to satisfy the requirements of the supervisory committee audit, verification of members' accounts and its additional responsibilities;

(ii) The credit union's accounting records and financial reports are promptly prepared and accurately reflect operations and results;

(iii) The relevant plans, policies, and control procedures established by the board of directors are properly administered; and

(iv) Policies and control procedures are sufficient to safeguard against error, carelessness, conflict of interest, self-dealing and fraud.

(c) *Supervisory committee audit.* (1) A supervisory committee audit of each Federal credit union shall occur at least once every calendar year and shall cover the period elapsed since the last audit period. The supervisory committee audit shall be performed by the supervisory committee or its designated representative, as prescribed in paragraph (c)(5) of this section.

(2) Standards for Performing Supervisory Committee Audit. The supervisory committee audit procedures/testing must be performed in accordance with the following standards:

(i) The audit is to be performed by a person or persons having adequate technical training and proficiency as an auditor commensurate with the level of sophistication and complexity of the credit union under audit.

(ii) Reasonable care is to be exercised in the performance of the audit and the preparation of the report.

(iii) The work is to be adequately planned and assistants, if any, are to be properly supervised.

(iv) The person or persons performing the audit must attain a sufficient understanding of the internal control structure to plan the audit and to determine the nature, timing, and extent of tests to be performed.

(v) The person or persons performing the audit must, through inspection, observation, inquiry, and confirmation obtain sufficient evidence to afford a reasonable basis for the financial statement elements, accounts or items under audit.

(3) Scope of Supervisory Committee Audit. The scope of the supervisory committee audit shall consist of:

(i) Attaining an understanding of the internal control structure;

(ii) Assessing the level of control risk; and

(iii) Based on the level of control risk, determining the nature, timing, and extent of substantive testing necessary to confirm the assertions made by management regarding each of assets, liabilities, equity, income, and expenses for the following attributes:

(A) Existence or occurrence;

(B) Completeness;

(C) Valuation or allocation;

(D) Rights and obligations; and

(E) Presentation and disclosures.

(4) In addition to scope requirements set forth in paragraph (c)(3) of this section, an audit performed by an independent, compensated auditor which includes any of the following areas must, with respect to audit scope but not with respect to reporting, satisfy GAAS for expressing an opinion on the financial statements taken as a whole:

(i) Internal controls;

(ii) Cash;

(iii) Loans and interest thereon;

(iv) Investments and interest thereon;

(v) Shares and dividends and/or interest thereon;

(vi) Related party transactions; and

(vii) The reporting of identified errors and irregularities with regard to each of the items in paragraphs (c)(4) (i) through (vi) of this section.

(5)(i) The requirements of the annual supervisory committee audit may be satisfied by one of the following:

(A) An opinion audit of the credit union's financial statements performed by an independent, licensed, certified public accountant;

(B) An "agreed-upon procedures engagement" performed by an independent, licensed, certified public accountant, which by itself or in combination with procedures performed by the supervisory committee, fulfills the required scope of the supervisory committee audit;

(C) A supervisory committee audit performed by an independent, compensated auditor other than an independent, licensed, certified public accountant which by itself or in combination with procedures performed by the supervisory committee, fulfills the scope of a supervisory committee audit; or

(D) A supervisory committee audit by the supervisory committee or its designated, uncompensated representative.

(ii) In all cases, an independent, compensated auditor is required to contract directly with the supervisory committee for the audit engagement and to deliver its written reports directly to the supervisory committee.

(iii) For a supervisory committee audit performed by the supervisory committee or its designated, uncompensated representative, the supervisory committee shall prepare a written report of the supervisory committee audit.

(d) *Engagement letter.* (1) The engagement of an independent, compensated auditor to perform all or a portion of the scope of a supervisory committee audit shall be evidenced by an engagement letter. The engagement letter shall be signed by the compensated auditor and acknowledged therein by the supervisory committee prior to commencement of a supervisory committee audit. The engagement letter shall:

(i) Specify the terms, conditions, and objectives of engagement;

(ii) Identify the basis of accounting to be used, e.g., GAAP or RAP;

(iii) Include an appendix setting forth the procedures to be performed (if not an opinion audit);

(iv) Specify the rate of, or total, compensation to be paid for the audit;

(v) Provided that the audit shall, upon completion of the engagement, deliver to the supervisory committee:

(A) A written report of the supervisory committee audit; and

(B) Notice in writing, either within the report or communicated separately, of any internal control reportable conditions and/or irregularities or illegal acts which come to the auditor's attention during the normal course of the audit (i.e., no additional duty is imposed nor additional written communications beyond (A) is required if none of these is noted);

(vi) Specify a target date of delivery of the written reports;

(vii) Certify that NCUA staff or its designated representative will be provided unconditional access to the complete set of original working papers either at the credit union or at a mutually agreeable location, for purposes of inspection; and

(viii) Acknowledge that working papers shall be retained for a minimum of three years from the date of the written audit report.

(2) In the case of a supervisory committee audit engagement which addresses all of the financial statement elements, accounts or items and attributes prescribed in paragraphs (c)(3) and (c)(4) of this section, the engagement letter shall certify that the contracted scope of the audit satisfies the requirements of a complete supervisory committee audit.

(3) In the case of a supervisory committee audit engagement which excludes any financial statement elements, accounts or items and attributes prescribed in paragraphs (c)(3) and (c)(4) of this section, the engagement letter shall:

(i) Identify the elements, accounts or items and attributes excluded from the audit;

(ii) State that, because of the exclusion(s), the resulting audit will not, by itself, fulfill the scope of a supervisory committee audit; and

(iii) Caution that the supervisory committee will remain responsible for fulfilling the scope of a supervisory committee audit with respect to the excluded elements, accounts or items and attributes.

(e) *Audit reports and working paper access.* (1) Upon completion or receipt of the written supervisory committee audit reports, the supervisory committee shall provide the reports to the board of directors. The supervisory committee shall ensure that the independent, compensated audit and its reports comply with the terms of the engage-

ment letter prescribed in this section. The supervisory committee shall, upon request, provide to the National Credit Union Administration a copy of the written reports received from the auditor.

(2) The supervisory committee shall be responsible for preparing and maintaining, or making available, a complete set of original working papers supporting each supervisory committee audit. The supervisory committee shall, upon request, provide NCUA staff unconditional access to such working papers either at the offices of the credit union or at a mutually agreeable location, for purposes of inspecting such working papers.

(f) *Sanctions.* (1) Failure of a supervisory committee and/or its independent compensated auditor to comply with the requirements of this section, or the terms of an engagement letter required by this section, is grounds for:

(i) The regional director to reject the supervisory committee audit;

(ii) The regional director to impose the remedies available in § 701.13, provided any of the conditions specified in § 701.13 is present; and

(iii) The NCUA to seek formal administrative sanctions against the supervisory committee and/or its independent, compensated auditor pursuant to section 206(r) of the Federal Credit Union Act, 12 U.S.C. 1786(r).

(2) In the case of a federally-insured state chartered credit union, NCUA shall provide the state regulator an opportunity to timely impose a remedy satisfactory to NCUA before seeking to impose a sanction permitted under (f)(1) of this section.

(g) Federal credit union compensated auditors, performing audits for supervisory committees, must be independent of the credit union's employees, members of the board of directors, supervisory and credit committees and/or the credit union's loan officers, and members of their immediate families. "Members of their immediate families" means a spouse, or a child, parent, grandchild, grandparent, brother or sister, or the spouse of any such individual.

(h)(1) The verification of members' accounts shall be made using any of the following methods:

(i) A controlled verification of 100 percent of members' share and loan accounts;

(ii) A sampling method that provides a random selection that is expected to be representative of the population from which the sample was selected, which will allow the auditor to test sufficient accounts in both number and scope to provide assurance that the General Ledger accounts are fairly stated in relation to the financial statements taken as a whole. When the auditor concludes that evidence provided by confirmations alone is not sufficient, additional procedures should be performed. That sampling procedure must provide each dollar in the population an equal chance of being selected;

(iii) *Independent, licensed, certified public accountants* are provided the additional option or sampling members' accounts using nonstatistical sampling methods consistent with *applicable* generally accepted auditing standards, provided the sampling method provides a selection that allows the auditor to test sufficient accounts in both number and scope to provide assurance that the General Ledger accounts are fairly stated in relation to the financial statements taken as a whole. When the auditor concludes that evidence provided by confirmations alone is not sufficient, additional procedures should be performed. Independent, licensed, certified public accountants will be responsible for documenting their sampling procedures, and providing evidence to NCUA, if requested, that the method used in consistent with *applicable* generally accepted auditing standards.

(2) Records of those accounts verified will be maintained and will be retained until the next verification of members' accounts is completed.

§ 701.13 Requirements for an Outside Audit.

(a) A Federal credit union shall obtain an outside, independent audit by a certified public accountant for any fiscal year during which any one of the following three conditions is present:

(1) the supervisory committee on the Federal credit union has not conducted an annual supervisory committee audit;

(2) the annual supervisory committee audit conducted did not meet the audit requirements of § 701.12 including § 701.12(h);

(3) the Federal credit union has experienced serious and persistent recordkeeping deficiencies as defined in Subsection (c) below.

(b) In the case of an audit required pursuant to condition (1) or (2) in paragraph (a) above, the scope of the outside, independent audit conducted by a certified public accountant must fully encompass the requirements set forth in § 701.12. In

the case of an audit required pursuant to condition (3) above, the outside, independent audit by a certified public accountant must be an opinion audit as that term is understood under generally accepted auditing standards.

(c) As used in condition (3) of paragraph (a) above, persistent recordkeeping deficiencies shall mean serious recordkeeping problems which continue to exist past a usual, expected, or normal period of time. Persistent recordkeeping deficiencies shall be considered serious if the Administration has a reasonable doubt that the financial condition of the credit union is accurately and fairly presented in the credit union's statements and that management practices and procedures are sufficient to safeguard members' assets.

§ 701.14 Change in Official or Senior Executive Officer in Credit Unions that are Newly Chartered or are in Troubled Condition.

(a) *Statement of Scope and Purpose.* Section 212 of the Federal Credit Union Act (12 U.S.C. 1790a) sets forth conditions under which a credit union must notify NCUA in writing of any proposed changes in its board of directors, committee members or senior executive staff. The regulation only applies in cases of newly chartered credit unions and credit unions in troubled condition.

(b) *Definitions.* For the purposes of this section:

(1) "Committee member" means any individual who serves as an official of the credit union in the capacity of a credit committee member or supervisory committee member.

(2) "Senior executive officer" means a credit union's chief executive officer (typically this individual holds the title of president or treasurer/manager), any assistant chief executive officer (e.g., any assistant president, any vice president or any assistant treasurer/manager) and the chief financial officer (controller). The term "senior executive officer" also includes employees of an entity, such as a consulting firm, hired to perform the functions of positions covered by the regulation.

(3) "Troubled condition" means any insured credit union that has one or a combination of the following conditions:

(i) Has been assigned

(A) A 4 or 5 CAMEL composite rating by the NCUA in the case of a federal credit union, or

(B) An equivalent 4 or 5 CAMEL composite rating by the state supervisor in the case of a federally insured, state-chartered credit union, or

(C) A 4 or 5 CAMEL composite rating by NCUA based on core workpapers received from the state supervisor in the case of a federally insured, state-chartered credit union in a state that does not use the CAMEL system. In this case, the state supervisor will be notified in writing by the Regional Director in the Region in which the credit union is located that the credit union has been designated by NCUA as a troubled institution;

(ii) Has been granted assistance as outlined under Sections 116 or 208 of the Federal Credit Union Act.

(c) *Prior Notice Requirement.* An insured credit union shall give NCUA written notice at least 30 days prior to the effective date of any addition or replacement of a member of the board of directors or committee member or the employment or change in responsibilities of any individual to a position as a senior executive officer if:

(1) The credit union has been chartered for less than 2 years; or

(2) The credit union meets the definition of troubled condition as set forth in paragraph 701.14(b)(3).

(d) *Procedures for Notice of Proposed Change in Official or Senior Executive Officer.*

(1) *Filing and acceptance.* Notices shall be filed with the appropriate Regional Director. State-chartered federally insured credit unions shall also file a copy of the notice with their state supervisor. The notice shall contain information pertaining to the competence, experience, character, or integrity of the individual with respect to whom the notice is submitted, subject to the authority of the Regional Director or his or her designee to require additional information. The information submitted must include the identity, personal history, business background, and experience of the individual, including material business activities and affiliations during the past 5 years, and a description of any material pending legal or administrative proceedings in which the individual is a party and any criminal indictment or conviction of such person by a state or Federal court. Each individual on whose behalf the notice is filed must attest to the validity of the information filed. At the option of the individual, the information may be forwarded to the Regional Director by the individual; however, in

such cases, the credit union must file a notice to that effect. The credit union submitting the notice shall be notified in writing of the date on which all required information is received and the notice is accepted for processing. Before the end of the 30-day period beginning on the date NCUA accepts the information for processing, the Regional Director will issue a written notice to the individual and the credit union of disapproval or approval of the proposed official or employee. If, after the 30-day period has ended, the individual has not been informed in writing of NCUA's disposition, the individual shall be considered approved.

(2) *Waiver of prior notice requirement.* Parties may petition the appropriate Regional Director for a waiver of the prior notice required under this Section. Waiver may be granted if it is found that delay could harm the credit union or the public interest. Any waiver shall not affect the authority of NCUA to issue a Notice of Disapproval within 30 days of the waiver, or within 30 days of any subsequent required notice.

(3) *Election of directors or credit committee members.*

(i) In the case of the election of a new member of the board of directors or credit committee member at a meeting of the members of a federally insured credit union, prior notice is not required. However, a completed notice must be filed with the appropriate Regional Director within 48 hours of the election.

(ii) If a director or credit committee member is disapproved by NCUA, the board of directors of the credit union may appoint its own alternate, to serve until the next annual meeting, contingent upon NCUA approval.

(e) *Commencement of service.* A proposed director, committee member or senior executive officer may begin to serve temporarily until the credit union and the individual are notified in writing of NCUA's approval or disapproval of the proposed addition or employment.

(f) *Notice of Disapproval.* NCUA may disapprove the individual's serving as a director, committee member or senior executive officer if it finds that the competence, experience, character, or integrity of the individual with respect to whom a notice under this section is submitted indicates that it would not be in the best interests of the members of the credit union or of the public to permit the individual to be employed by, or associated with, the credit union. The Notice of Disapproval will advise the parties of their rights of appeal pursuant to 12 CFR Part 747 subpart J of NCUA's Regulations.

§§ 701.15–701.18 [Reserved]

§ 701.19 Retirement Benefits for Employees of Federal Credit Unions.

(a) A Federal credit union may make provision for reasonable retirement benefits for its employees and for officers who are compensated in conformance with the Act and the bylaws, either individually or collectively with other credit unions. In those cases where a Federal credit union is to be a plan trustee or custodian, the plan must be authorized and maintained in accordance with the provisions of part 724 of this chapter. Where the trustee or custodian is a party other than the Federal credit union, the employee benefit plan must be maintained in accordance with the applicable laws governing employee benefit plans and such rules and regulations as may be promulgated by the Secretary of Labor, the Secretary of the Treasury, or any other Federal or state authority exercising jurisdiction over such plans.

(b) No Federal credit union shall occupy the position of a fiduciary, as defined in the Employee Retirement Income Security Act of 1974 and rules and regulations promulgated thereunder by the Secretary of Labor, unless provision has been made for appropriate liability insurance as provided under Section 410(b) of the Employee Retirement Income Security Act of 1974.

§ 701.20 Fidelity Bond and Insurance Coverage for Federal Credit Unions.

(a) *Scope.* This Part provides the requirements for fidelity bonds for Federal credit union employees and officials and for general insurance coverage for losses caused by persons outside of the credit union (protection for losses due to theft, holdup, vandalism, etc.).

(b) *Review of Coverage.* The board of directors of each Federal credit union shall, at least annually, carefully review the bond and insurance coverage in force in order to ascertain its adequacy in relation to risk exposure and to the minimum requirements fixed from time to time by the NCUA Board.

(c) *Minimum Coverage; Approved Forms.* Every Federal credit union will maintain bond and insurance coverage with a company holding a certificate of authority from the Secretary of the Treasury. Credit Union Blanket Bond Standard Form No. 23 of the Surety Association of America (revised to May, 1950) is considered the minimum coverage required and is approved. Credit Union Blanket Bond Forms 581 and 582 are also approved. Any other basic bond forms, and all riders and endorsements which limit the coverage provided by approved bond forms, must receive the prior written approval of the NCUA Board. Fidelity bonds must provide coverage for the fraud or dishonesty of all employees, directors, officers, and supervisory and credit committee members. Notwithstanding the foregoing, effective January 1, 1990 all bonds must include a provision, in a form approved by the NCUA Board, requiring written notification by surety to the Board: (1) when the bond of a credit union is terminated in its entirety; or (2) when bond coverage is terminated, by issuance of a written notice, on an employee, director, officer, supervisory or credit committee member. Said notification shall be sent to the Secretary of the NCUA Board or designee and shall include a brief statement of cause for termination.

(d) *Minimum Coverage Amounts.* The minimum amount of bond coverage required will be computed based on the Federal credit union's total assets. The following table lists the minimum requirements:

Assets	Minimum Bond
$0 to $10,000	Coverage equal to the credit union's assets.
$10,001 to $1,000,000	$10,000 for each $100,000 or fraction thereof.
$1,000,001 to $50,000,000	$100,000 plus $50,000 for each million or fraction over $1,000,000.
$50,000,001 to $295,000,000	$2,550,000 plus $10,000 for each million or fraction thereof over $50,000,000.
Over $295,000,000	$5,000,000.

It is the duty of the board of directors of each Federal credit union to provide adequate protection to meet its unique circumstances by obtaining, when necessary, bond and insurance coverage in excess of the above minimums.

(e) *Increased Coverage, Cash on Hand or in Transit.* When either of the following amounts exceed a Federal credit union's minimum coverage limits as specified in paragraph (d) of this regulation, the minimum coverage limits for that Federal credit union will be increased to be equal to the greater of the following amounts within thirty days of the discovery of the need for such increase:

(1) The aggregate amount of the daily cash fund (change fund plus maximum anticipated daily money receipts) and food stamps (if any), on the Federal credit union's premises, or

(2) The aggregate amount of the Federal credit union's money and food stamps (if any) placed in transit in any one individual shipment.

For purposes of this Section, the term "money" shall include currency, coin, banknotes, Federal Reserve notes, revenue stamps and postage stamps.

(f) *Increased Cash Coverage; Exception.* Subsection (e) notwithstanding, no increase in coverage will be required where a Federal credit union temporarily increases its cash fund because of an extraordinary event which reasonably cannot be expected to recur.

(g) *Reduced Coverage; NCUA Approval.* Any proposal for reduced coverage must be approved in writing by the NCUA Board at least twenty days in advance of the proposed effective date of the reduction.

(h) *Deductibles.*

(1) The maximum amount of deductibles allowed are based on the Federal credit union's total assets. The following table sets out the maximum deductibles:

Assets	Minimum Bond
$0–$100,000	No deductibles allowed
$100,001–$250,000	$1,000.
$250,001–$1,000,000	$2,000.
Over $1,000,001	$2,000 plus 1/1000 of total assets up to a maximum deductible of $200,000.

(2) A deductible may be applied separately to one or more insuring clauses in a blanket bond. Deductibles in excess of those shown in this Section must have the written approval of the NCUA Board at least twenty days prior to the effective date of such deductibles.

(3) No deductible will exceed ten percent of a Federal credit union's Regular Reserve unless the credit union creates a segregated Contingency Reserve for the amount of the excess. Valuation allowance accounts, e.g., allowance for loan losses, may not be considered part of the Regular Reserve when determining the maximum deductible.

(i) *Additional Coverage.* The NCUA Board may require additional coverage for any Federal credit union when, in the opinion of the Board, current coverage is insufficient. The board of directors of the Federal credit union must obtain additional

coverage within thirty days after the date of written notice from the NCUA Board.

§ 701.21 Loans to Members and Lines of Credit to Members.

(a) *Statement of Scope and Purpose.* Section 701.21 complements the provisions of Section 107(5) of the Federal Credit Union Act (12 U.S.C. § 1757(5)) authorizing Federal credit unions to make loans to members and issue lines of credit (including credit cards) to members. Section 107(5) of the Act contains limitations on matters such as loan maturity, rate of interest, security, and prepayment penalties. Section 701.21 interprets and implements those provisions. In addition, Section 701.21 states the NCUA Board's intent concerning preemption of state laws, and expands the authority of Federal credit unions to enforce due-on-sale clauses in real property loans. Also, while § 701.21 generally applies to Federal credit unions only, its provisions may be used by state-chartered credit unions with respect to alternative mortgage transactions in accordance with 12 U.S.C. 3801 *et seq.*, and certain provisions apply to loans made by federally insured state-chartered credit unions as specified in § 741.203 of this chapter. Part 722 sets forth requirements for appraisals for certain real estate-secured loans made under Section 701.21 and any other applicable lending authority. Finally, it is noted that Section 701.21 does not apply to loans by Federal credit unions to other credit unions (although certain statutory limitations in Section 107 of the Act apply), nor to loans to credit union organizations (which are governed by Section 107(5)(D) of the Act and Section 701.27 of this Part.

(b) *Relation to Other Laws:*

(1) *Preemption of state laws.* Section 701.21 is promulgated pursuant to the NCUA Board's exclusive authority as set forth in Section 107(5) of the Federal Credit Union Act (12 U.S.C. § 1757(5)) to regulate the rates, terms of repayment and other conditions of Federal credit union loans and lines of credit (including credit cards) to members. This exercise of the Board's authority preempts any state law purporting to limit or affect:

(i) (A) rates of interest and amounts of finance charges, including:

(1) the frequency or the increments by which a variable interest rate may be changed;

(2) the index to which a variable interest rate may be tied;

(3) the manner or timing of notifying the borrower of a change in interest rate;

(4) the authority to increase the interest rate on an existing balance;

(B) late charges; and

(C) closing costs, application, origination, or other fees;

(ii) terms of repayment, including:

(A) the maturity of loans and lines of credit;

(B) the amount, uniformity, and frequency of payments, including the accrual of unpaid interest if payments are insufficient to pay all interest due;

(C) balloon payments; and

(D) prepayment limits;

(iii) conditions related to:

(A) the amount of the loan or line of credit;

(B) the purpose of the loan or line of credit;

(C) the type or amount of security and the relation of the value of the security to the amount of the loan or line of credit;

(D) eligible borrowers; and

(E) the imposition and enforcement of liens on the shares of borrowers and accommodation parties.

(2) *Matters not preempted.* Except as provided by Section 701.21(b)(1), it is not the Board's intent to preempt state laws that do not affect rates, terms of repayment and other conditions described above concerning loans and lines of credit, for example:

(i) insurance laws;

(ii) laws related to transfer of and security interests in real and personal property (see, however, paragraph (g)(6) of this section concerning the use and exercise of due-on-sale clauses);

(iii) conditions related to:

(A) collection costs and attorneys' fees;

(B) requirements that consumer lending documents be in "plain language"; and

(C) the circumstances in which a borrower may be declared in default and may cure default.

(3) *Other Federal law.* Except as provided by Section 701.21(b)(1), it is not the Board's intent to preempt state laws affecting aspects of credit transactions that are primarily regulated by Federal law other than the Federal Credit Union Act, for example, state laws concerning

credit cost disclosure requirements, credit discrimination, credit reporting practices, unfair credit practices, and debt collection practices. Applicability of state law in these instances should be determined pursuant to the preemption standards of the relevant Federal law and regulations.

(4) *Examination and Enforcement.* Except as otherwise agreed by the NCUA Board, the Board retains exclusive examination and administrative enforcement jurisdiction over Federal credit unions. Violations of Federal or applicable state laws related to the lending activities of a Federal credit union should be referred to the appropriate NCUA regional office.

(5) *Definition of State Law.* For purposes of Section 701.21(b) "state law" means the constitution, laws, regulations and judicial decisions of any state, the District of Columbia, the several territories and possessions of the United States, and the Commonwealth of Puerto Rico.

(c) *General Rules:*

(1) *Scope.* The following general rules apply to all loans to members and, where indicated, all lines of credit (including credit cards) to members, except as otherwise provided in the remaining provisions of Section 701.21.

(2) *Written policies.* The board of directors of each Federal credit union shall establish written policies for loans and lines of credit consistent with the relevant provisions of the Act, NCUA's regulations, and other applicable laws and regulations.

(3) *Credit application.* Consistent with policies established by the board of directors, the credit committee or loan officer shall ensure that a credit application is kept on file for each borrower supporting the decision to make a loan or establish a line of credit.

(4) *Maturity.* The maturity of a loan to a member may not exceed 12 years. Lines of credit are not subject to a statutory or regulatory maturity limit. Amortization of line of credit balances and the type and amount of security on any line of credit shall be as determined by contract between the Federal credit union and the member/borrower.

(5) *Ten percent limit.* No loan or line of credit advance may be made to any member if such loan or advance would cause that member to be indebted to the Federal credit union upon loans and advances made to the member in an aggregated amount exceeding 10% of the credit union's total unimpaired shares and surplus. In the case of member business loans as defined in § 723.1 of this chapter. Additional limitations apply as set forth in §§ 723.8 and 723.9 of this chapter.

(6) *Early payment.* A member may repay a loan, or outstanding balance on a line of credit, prior to maturity in whole or in part on any business day without penalty.

(7) *Loan interest rates.*

(i) *General.* Except when a higher maximum rate is provided for in 701.21(c)(7)(ii), a Federal credit union may extend credit to its members at rates not to exceed 15 percent per year on the unpaid balance inclusive of all finance charges. Variable rates are permitted on the condition that the effective rate over the term of the loan (or line of credit) does not exceed the maximum permissible rate.

(ii) *Temporary rates.—(A) 21 percent maximum rate.* Effective from December 3, 1980 through May 14, 1987, a Federal credit union may extend credit to its members at rates not to exceed 21 percent per year on the unpaid balance inclusive of all finance charges. Loans and line of credit balances existing on or before May 14, 1987, may continue to bear rates of interest of up to 21 percent per year after May 14, 1987.

(B) *18 percent maximum rate.* Effective May 15, 1987, a Federal credit union may extend credit to its members at rates not to exceed 18 percent per year on the unpaid balance inclusive of all finance charges.

(C) *Expiration.* After September 9, 2000, or as otherwise ordered by the NCUA Board, the maximum rate on federal credit union extensions of credit to members shall revert to 15 percent per year. Higher rates may, however, be charged, in accordance with paragraphs (c)(7)(ii) (A) and (B) of this section, on loans and line of credit balances existing on or before May 16, 1987.

(8)(i) Except as otherwise provided herein, no official or employee of a Federal credit union, or immediate family member of an official or employee of a Federal credit union, may receive, directly or indirectly, any commission, fee, or other compensation in connection with any loan made by the credit union.

(ii) For the purposes of this section:

Compensation includes non monetary items, except those of nominal value.

Immediate family member means a spouse or other family member living in the same household.

Loan includes line of credit.

Official means any member of the board of directors or a volunteer committee.

Person means an individual or an organization.

Senior management employee means the credit union's chief executive officer (typically, this individual holds the title of President or Treasurer/Manager), any assistant chief executive officers (e.g., Assistant President, Vice President, or Assistant Treasurer/Manager), and the chief financial officer (Comptroller).

Volunteer official means an official of a credit union who does not receive compensation from the credit union solely for his or her service as an official.

(iii) This section does not prohibit:

(A) Payment, by a Federal credit union, of salary to employees;

(B) Payment, by a Federal credit union, of an incentive or bonus to an employee based on the credit union's overall financial performance;

(C) Payment, by a Federal credit union, of an incentive or bonus to an employee, other than a senior management employee, in connection with a loan or loans made by the credit union, provided that the board of directors of the credit union establishes written policies and internal controls in connection with such incentive or bonus and monitors compliance with such policies and controls at least annually.

(D) Receipt of compensation from a person outside a Federal credit union by a volunteer official or non senior management employee of the credit union, or an immediate family member of a volunteer official or employee of the credit union, for a service or activity performed outside the credit union, provided that no referral has been made by the credit union or the official, employee, or family member.

(d) *Loans and Lines of Credit to Officials:*

(1) *Purpose.* Sections 107(5)(A) (iv) and (v) of the Act require the approval of the board of directors of the Federal credit union in any case where the aggregate of loans to an official and loans on which that official serves as endorser or guarantor exceeds $20,000 plus pledged shares. This Section (701.21(d)) implements the requirement by establishing procedures for determining whether board of directors' approval is required. The section also prohibits preferential treatment of officials.

(2) *Official.* An "official" is any member of the board of directors, credit committee or supervisory committee.

(3) *Initial approval.* All applications for loan or lines of credit on which an official will be either a direct obligor or an endorser, cosigner or guarantor shall be initially acted upon by either the board of directors, the credit committee or loan officer, as specified in the Federal credit union's bylaws.

(4) *Board of directors' review.* The board of directors shall, in any case, review and approve or deny an application on which an official is a direct obligor, or endorser, cosigner or guarantor if the following computation produces a total in excess of $20,000:

(i) Add:

(A) The amount of the current application.

(B) The outstanding balances of loans including the used portion of an approved line of credit, extended to or endorsed, cosigned or guaranteed by the official.

(C) The total unused portion of approved lines of credit extended to or endorsed, cosigned or guaranteed by the official.

(ii) From the above total subtract:

(A) the amount of shares pledged by the official on loans or lines of credit extended to or endorsed, cosigned or guaranteed by the official.

(B) The amount of shares to be pledged by the official on the loan or line of credit applied for.

(5) *Nonpreferential treatment.* The rates, terms and conditions on any loan or line of credit either made to, or endorsed or guaranteed by

(i) an official

(ii) an immediate family member of an official, or

(iii) any individual having a common ownership, investment or other pecuniary interest in a business enterprise with an official or with an immediate family member of an official shall not be more favorable than the rates, terms and conditions for comparable loans or lines of credit to other credit union members. "Immediate family members" means a spouse or other family member living in the same household.

(e) *Insured, Guaranteed and Advance Commitment Loans.* A loan secured by the insurance or guarantee of, or with an advance commitment to purchase the loan by, the Federal Government, a State government, or any agency of either, may

be made for the maturity and under the terms and conditions, including rate of interest, specified in the law, regulations or program under which the insurance, guarantee or commitment is provided.

(f) *20-Year Loans.* Notwithstanding the general 12-year maturity limit on loans to members, a Federal credit union may make loans with maturities of up to 20 years in the case of: (1) a loan to finance the purchase of a mobile home if the mobile home will be used as the member-borrower's residence and the loan is secured by a first lien on the mobile home, (2) a second mortgage loan (or a nonpurchase money first mortgage loan in the case of a residence on which there is no existing first mortgage) if the loan is secured by a residential dwelling which is the residence of the member-borrower, and (3) a loan to finance the repair, alteration, or improvement of a residential dwelling which is the residence of the member-borrower.

(g) *Long-Term Mortgage Loans:*

(1) *Authority.* A Federal credit union may make residential real estate loans to members, with maturities of up to 40 years, or such longer period as may be permitted by the NCUA Board on a case-by-case basis, subject to the conditions of this Section (701.21(g)).

(2) *Statutory limits.* The loan shall be made on a one- to four-family dwelling that is or will be the principal residence of the member-borrower and the loan shall be secured by a perfected first lien in favor of the credit union on such dwelling (or a perfected first security interest in the case of either a residential cooperative or a leasehold or ground rent estate).

(3) *Loan application.* The loan application shall be a completed standard Federal Housing Administration, Veterans Administration, Federal Home Loan Mortgage Corporation, Federal National Mortgage Association or Federal Home Loan Mortgage Corporation/Federal National Mortgage Association application form. In lieu of use of a standard application the Federal credit union may have a current attorney's opinion on file stating that the forms in use meet the requirements of applicable Federal, state and local laws.

(4) *Security instrument and note.* The security instrument and note shall be executed on the most current version of the FHA, VA, FHLMC, FNMA, or FHLMC/FNMA Uniform Instruments for the jurisdiction in which the property is located. No prepayment penalty shall be allowed, although a Federal credit union may require that any partial prepayments be made on the date monthly installments are due and be in the amount of that part of one or more monthly installments that would be applicable to principal. In lieu of use of a standard security instrument and note, the Federal credit union may have a current attorney's opinion on file stating that the security instrument and note in use meet the requirements of applicable Federal, state and local laws.

(5) *First lien, territorial limits.* The loan shall be secured by a perfected first lien or first security interest in favor of the credit union supported by a properly executed and recorded security instrument. No loan shall be secured by a residence located outside the United States of America, its territories and possessions, or the Commonwealth of Puerto Rico.

(6) *Due-on-sale clauses:*

(i) Except as otherwise provided herein, the exercise of a due-on-sale clause by a Federal credit union is governed exclusively by Section 341 of Public Law 97–320 and by any regulations issued by the Federal Home Loan Bank Board implementing Section 341.

(ii) In the case of a contract involving a long-term (greater than twelve years), fixed rate first mortgage loan which was made or assumed, including a transfer of the liened property subject to the loan, during the period beginning on the date a state adopted a constitutional provision or statute prohibiting the exercise of due-on-sale clauses, or the date on which the highest court of such state has rendered a decision (or if the highest court has not so decided, the date on which the next highest court has rendered a decision resulting in a final judgment if such decision applies statewide) prohibiting such exercise, and ending on October 15, 1982, a Federal credit union may exercise a due-on-sale clause in the case of a transfer which occurs on or after November 18, 1982, unless exercise of the due-on-sale clause would be based on any of the following:

(A) the creation of a lien or other encumbrance subordinate to the lender's security instrument which does not relate to a transfer of rights of occupancy in the property;

(B) the creation of a purchase money security interest for household appliances;

(C) a transfer by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety;

(D) the granting of a leasehold interest of 3 years or less not containing an option to purchase;

(E) a transfer to a relative resulting from the death of a borrower;

(F) a transfer where the spouse or children of the borrower become an owner of the property;

(G) a transfer resulting from a decree of a dissolution of marriage, a legal separation agreement, or from an incidental property settlement agreement, by which the spouse of the borrower becomes an owner of the property;

(H) a transfer into an inter vivos trust in which the borrower is and remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property; or

(I) any other transfer or disposition described in regulations promulgated by the Federal Home Loan Bank Board.

(7) *Assumption of real estate loans by nonmembers.* A federal credit union may permit a nonmember to assume a member's mortgage loan in conjunction with the nonmember's purchase of the member's principal residence, provided that the nonmember assumes only the remaining unpaid balance of the loan, the terms of the loan remain unchanged, and there is no extension of the original maturity date specified in the loan agreement with the member. An assumption is impermissible if the original loan was made with the intent of having a nonmember assume the loan.

(h) *Removed and replaced by part 723.*

(i) *Put Option Purchases in Managing Increased Interest-Rate Risk for Real Estate Loans Produced for Sale on the Secondary Market.*

(1) *Definitions.* For purposes of this § 701.21(i):

(i) "Financial options contact" means an agreement to make or take delivery of a standardized financial instrument upon demand by the holder of the contract at any time prior to the expiration date specified in the agreement, under terms and conditions established either by (A) a contract market designated for trading such contracts by the Commodity Futures Trading Commission, or (B) by a Federal credit union and a primary dealer in Government securities that are counterparties in an over-the-counter transaction.

(ii) "FHLMC security" means obligations or other securities which are or ever have been sold by the Federal Home Loan Mortgage Corporation pursuant to Sections 305 or 306 of the Federal Home Loan Mortgage Corporation Act (12 U.S.C. §§ 1454 and 1455).

(iii) "FNMA security" means an obligation, participation, or any instrument of or issued by, or fully guaranteed as to principal and interest by, the Federal National Mortgage Association.

(iv) "GNMA security" means an obligation, participation, or any instrument of or issued by, or fully guaranteed as to principal and interest by, the Government National Mortgage Association.

(v) "Long position" means the holding of a financial options contract with the option to make or take delivery of a financial instrument.

(vi) "Primary dealer in Government securities" means: (A) a member of the Association of Primary Dealers in United States Government Securities; or (B) any parent, subsidiary, or affiliated entity of such primary dealer where the member guarantees (to the satisfaction of the FCU's board of directors) over-the-counter sales of financial options contracts by the parent, subsidiary, or affiliated entity to a Federal credit union.

(vii) "Put" means a financial options contract which entitles the holder to sell, entirely at the holder's option, a specified quantity of a security at a specified price at any time until the stated expiration date of the contract.

(2) *Permitted Options Transactions.* A Federal credit union may, to manage risk of loss through a decrease in value of its commitments to originate real estate loans at specified interest rates, enter into long put positions on GNMA, FNMA, and FHLMC securities:

(i) if the real estate loans are to be sold on the secondary market within ninety (90) days of closing;

(ii) if the positions are entered into: (A) through a contract market designated by the Commodity Futures Trading Commission for trading such contracts, or (B) with a primary dealer in Government securities;

(iii) if the positions are entered into pursuant to written policies and procedures which are approved by the Federal credit union's board of directors, and include, at a minimum: (A) the Federal credit union's strategy in using financial options contracts and its analysis of how the strategy will reduce sensitivity to changes in price or interest rates in its commitments to originate real estate loans at specified interest rates; (B) a list of brokers or other intermediaries through which positions

may be entered into; (C) quantitative limits (e.g., position and stop loss limits) on the use of financial options contracts; (D) identification of the persons involved in financial options contract transactions, including a description of these persons' qualifications, duties, and limits of authority, and description of the procedures for segregating these persons' duties, (E) a requirement for written reports for review by the Federal credit union's board of directors at its monthly meetings, or by a committee appointed by the board on a monthly basis, of: (1) the type, amount, expiration date, correlation, cost of, and current or projected income or loss from each position closed since the last board review, each position currently open and current gains or losses from such positions, and each position planned to be entered into prior to the next board review; (2) compliance with limits established on the policies and procedures; and (3) the extent to which the positions described contributed to reduction of sensitivity to changes in prices or interest rates in the Federal credit union's commitments to originate real estate loans at a specified interest rate; and

(iv) if the Federal credit union has received written permission from the appropriate NCUA Regional Director to engage in financial options contracts transactions in accordance with this § 701.21(i) and its policies and procedures as written.

(3) *Recordkeeping and Reporting.*

(i) The reports described in § 701.21 (i)(2)(iii)(E) for each month must be submitted to the appropriate NCUA Regional Office by the end of the following month. This monthly reporting requirement may be waived by the appropriate NCUA Regional Director on a case-by-case basis for those Federal credit unions with a proven record of responsible use of permitted financial options contracts.

(ii) The records described in § 701.21 (i)(2)(iii)(E) must be retained for two years from the date the financial options contracts are closed.

(4) *Accounting.* A Federal credit union must account for financial options contracts transactions:

(i) in accordance with standards established by the NCUA Board in the Accounting Manual for Federal Credit Unions, available from NCUA, Administrative Office, 1775 Duke Street, Alexandria, VA 22314, or such other instruction as may be deemed appropriate; or

(ii) to the extent not inconsistent with NCUA Board instructions, in accordance with generally accepted accounting standards or principles.

§ 701.22 Loan Participation.

(a) For purposes of this section:

(1) "Participation loan" means a loan where one or more eligible organizations participates pursuant to a written agreement with the originating lender.

(2) "Eligible organizations" means a credit union, credit union organization, or financial organization.

(3) "Credit union" means any Federal or state chartered credit union.

(4) "Credit union organization" means any organization as determined by the Board, established primarily to serve the daily operational needs of its member credit unions. The term does not include trade associations, membership organizations principally composed of credit unions, or corporations or other businesses which principally provide services to credit union members as opposed to corporations or businesses whose business relates to the daily in-house operation of credit unions.

(5) "Financial organization" means any federally chartered or federally insured financial institution.

(6) "Originating lender" means the participant with which the member contracts.

(b) Subject to the provisions of this section any Federal credit union may participate in making loans with eligible organizations within the limitations of the board of directors' written participation loan policies, PROVIDED:

(1) no Federal credit union shall obtain an interest in a participation loan if the sum of that interest and any (other) indebtedness owing to the Federal credit union by the borrower exceeds 10 per centum of the Federal credit union's unimpaired capital and surplus;

(2) a written master participation agreement shall be properly executed, acted upon by the Federal credit union's board of directors, or if the board has so delegated in its policy, the investment committee or senior management offical(s) and retained in the Federal credit union's office. The master agreement shall include provisions for identifying, either through a document which is incorporated by reference into the master agreement, or directly in the

master agreement, the participation loan or loans prior to their sale; and

(3) a Federal credit union may sell to or purchase from any participant the servicing of any loan in which it owns a participation interest.

(c) An originating lender which is a Federal credit union shall:

(1) originate loans only to its members;

(2) retain an interest of at least 10 per centum of the face amount of each loan;

(3) retain the original or copies of the loan documents; and

(4) Require the credit committee or loan officer to use the same underwriting standards for participation loans used for loans that are not being sold in a participation agreement unless there is a participation agreement in place prior to the disbursement of the loan. Where a participation agreement is in place prior to disbursement, either the credit union's loan policies or the participation agreement shall address any variance from non-participation loan underwriting standards.

(d) A participant Federal credit union that is not an originating lender shall:

(1) participate only in loans it is empowered to grant, having a participation policy in place which sets forth the loan underwriting standards prior to entering into a participation agreement;

(2) participate in participation loans only if made to its own members or members of another participating credit union;

(3) retain the original or a copy of the written participation loan agreement and a schedule of the loans covered by the agreement; and

(4) obtain the approval of the board of directors or investment committee of the disbursement of proceeds to the originating lender.

§ 701.23 Purchase, Sale, and Pledge of Eligible Obligations.

(a) For purposes of this Section:

(1) "Eligible obligation" means a loan or group of loans;

(2) "Student loan" means a loan granted to finance the borrower's attendance at an institution of higher education or at a vocational school, which is secured by and on which payment of the outstanding principal and interest has been deferred in accordance with the insurance or guarantee of the Federal Government, of a State government, or any agency of either.

(b) Purchase.

(1) A Federal credit union may purchase, in whole or in part, within the limitations of the board of directors' written purchase policies:

(i) Eligible obligations of its members, from any source, if either (A) they are loans it is empowered to grant or (B) they are refinanced with the consent of the borrowers, within 60 days after they are purchased, so that they are loans it is empowered to grant;

(ii) Eligible obligations of a liquidating credit union's individual members, from the liquidating credit union;

(iii) Student loans, from any source, if the purchaser is granting student loans on an ongoing basis and if the purchase will facilitate the purchasing credit union's packaging of a pool of such loans to be sold or pledged on the secondary market; and

(iv) Real estate-secured loans, from any source, if the purchaser is granting real estate secured loans pursuant to Section 701.21 on an ongoing basis and if the purchase will facilitate the purchasing credit union's packaging of a pool of such loans to be sold or pledged on the secondary mortgage market. A pool must include a substantial portion of the credit union's members' loans and must be sold promptly.

(2) A Federal credit union may make purchases in accordance with this paragraph (b), provided:

(i) the board of directors or investment committee approves the purchase;

(ii) a written agreement and a schedule of the eligible obligations covered by the agreement are retained in the purchaser's office; and for purchases under paragraph (b)(1)(ii) of this section, any advance written approval required by § 741.8 of this chapter is obtained before consummation of such purchase.

(3) The aggregate of the unpaid balance of eligible obligations purchased under paragraph (b) of this section cannot exceed 5% of the unimpaired capital and surplus of the purchaser. The following can be excluded in calculating this 5% limitation:

(i) Student loans purchased in accordance with paragraph (b)(1)(iii) of this section;

(ii) Real estate loans purchased in accordance with paragraph (b)(1)(iv) of this section;

(iii) Eligible obligations purchased in accordance with paragraph (b)(1)(i) of this sec-

tion that are refinanced by the purchaser so that it is a loan it is empowered to grant; and

(iv) An indirect lending or indirect leasing arrangement that is classified as a loan and not the purchase of an eligible obligation because the federal credit union makes the final underwriting decision and the sales or lease contract is assigned to the federal credit union very soon after it is signed by the member and the dealer or leasing company.

(c) Sale.

(1) A Federal credit union may sell, in whole or in part, to any source, eligible obligations of its members, eligible obligations purchased in accordance with subsection (b)(1)(ii), student loans purchased in accordance with subsection (b)(1)(iii), and real estate loans purchased in accordance with subsection (b)(1)(iv), within the limitations of the board of directors' written sale policies, provided:

(i) The board of directors or investment committee approves the sale; and

(ii) A written agreement and a schedule of the eligible obligations covered by the agreement are retained in the seller's office.

(d) Pledge.

(1) A Federal credit union may pledge, in whole or in part, to any source, eligible obligations of its members, eligible obligations purchased in accordance with subsection (b)(1)(ii), student loans purchased in accordance with subsection (b)(1)(iii), and real estate loans purchased in accordance with subsection (b)(1)(iv), within the limitations of the board of directors' written pledge policies, provided:

(i) The board of directors or investment committee approves the pledge;

(ii) Copies of the original loan documents are retained; and

(iii) A written agreement covering the pledging arrangement is retained in the office of the credit union that pledges the eligible obligations.

(2) The pledge agreement shall identify the eligible obligations covered by the agreement.

(e) Servicing.

A Federal credit union may agree to service any eligible obligation it purchases or sells in whole or in part.

(f) 10 Percent Limitation.

The total indebtedness owing to any Federal credit union by any person, inclusive of retained and reacquired interests, shall not exceed 10 percent of its unimpaired capital and surplus.

§ 701.24 Refund of Interest.

(a) The board of directors of a Federal credit union may authorize an interest refund to members who paid interest to the credit union during any dividend period and who are members of record at the close of business on the last day of such dividend period. Interest refunds may be made for a dividend period only if dividends on share accounts have been declared and paid for that period.

(b) The amount of interest refund to each member shall be determined as a percentage of the interest paid by the member. Such percentage may vary according to the type of extension of credit and the interest rate charged.

(c) The board of directors may exclude from an interest refund: (1) a particular type of extension of credit; (2) any extension of credit made at a particular interest rate; and (3) any extension of credit that is presently delinquent or has been delinquent within the period for which the refund is being made.

§ 701.25 [Reserved]

§ 701.26 Credit Union Service Contracts.

A Federal credit union may act as a representative of and enter into a contractual agreement with one or more credit unions or other organizations for the purpose of sharing, utilizing, renting, leasing, purchasing, selling, and/or joint ownership of fixed assets or engaging in activities and/or services which relate to the daily operations of credit unions. Agreements must be in writing, and shall advise all parties subject to the agreement that the goods and services provided shall be subject to examination by the NCUA Board to the extent permitted by law.

§ 701.27 [Removed April 1998, replaced by new part 712]

§§ 701.28–701.29 [Reserved]

§ 701.30 Safe Deposit Box Service.

A Federal credit union may lease safe deposit boxes to its members.

§ 701.31 Nondiscrimination Requirements.

(a) *Definitions:* As used in this part, the term:

(1) "application" carries the meaning of that term as defined in 12 C.F.R. 202.2(f) (Regula-

tion B), which is as follows: "An oral or written request for an extension of credit that is made in accordance with procedures established by a creditor for the type of credit requested";

(2) "dwelling" carries the meaning of that term as defined in 42 U.S.C. 3602(b) (Fair Housing Act), which is as follows: "Any building, structure, or portion thereof which is occupied as, or designed or intended for occupancy as, a residence by one or more families, and any vacant land which is offered for sale or lease for the construction or location thereon of any building, structure, or portion thereof"; and

(3) "real estate-related loan" means any loan for which application is made to finance or refinance the purchase, construction, improvement, repair, or maintenance of a dwelling.

(b) *Nondiscrimination in Lending:*

(1) A Federal credit union may not deny a real estate-related loan, nor may it discriminate in setting or exercising its rights pursuant to the terms or conditions of such a loan, nor may it discourage an application for such a loan, on the basis of the race, color, national origin, religion, sex, handicap, or familial status (having children under the age of 18) of:

(i) any applicant or joint applicant;

(ii) any person associated, in connection with a real estate-related loan application, with an applicant or joint applicant;

(iii) the present or prospective owners, lessees, tenants, or occupants of the dwelling for which a real estate-related loan is requested;

(iv) the present or prospective owners, lessees, tenants, or occupants of other dwellings in the vicinity of the dwelling for which a real estate-related loan is requested.

(2) With regard to a real estate-related loan, a Federal credit union may not consider a lending criterion or exercise a lending policy which has the effect of discriminating on the basis of race, color, national origin, religion, sex, handicap, or familial status (having children under the age of 18). Guidelines concerning possible exceptions to this provision appear in paragraph (e)(1) of this section.

(3) Consideration of any of the following factors in connection with a real estate-related loan is not necessary to a Federal credit union's business, generally has a discriminatory effect, and is therefore prohibited:

(i) the age or location of the dwelling;

(ii) zip code of the applicant's current residence;

(iii) previous home ownership;

(iv) the age or location of dwellings in the neighborhood of the dwelling;

(v) the income level of residents in the neighborhood of the dwelling;

Guidelines concerning possible exceptions to this provision appear in paragraph (e)(2) of this section.

(c) *Nondiscrimination in Appraisals:*

(1) A Federal credit union may not rely upon an appraisal of a dwelling if it knows or should know that the appraisal is based upon consideration of the race, color, national origin, religion, sex, handicap, or familial status (having children under the age of 18) of:

(i) any applicant or joint applicant;

(ii) any person associated, in connection with a real estate-related loan application, with an applicant or joint applicant;

(iii) the present or prospective owners, lessees, tenants, or occupants of the dwelling for which a real estate-related loan is requested;

(iv) the present or prospective owners, lessees, tenants, or occupants of other dwellings in the vicinity of the dwelling for which a real estate-related loan is requested.

(2) With respect to a real estate-related loan, a Federal credit union may not rely upon an appraisal of a dwelling if it knows or should know that the appraisal is based upon consideration of a criterion which has the effect of discriminating on the basis of race, color, national origin, religion, sex, handicap, or familial status (having children under the age of 18). Guidelines concerning possible exceptions to this provision appear in paragraph (e)(1) of this section.

(3) A Federal credit union may not rely upon an appraisal that it knows or should know is based upon consideration of any of the following criteria, for such criteria generally have a discriminatory effect, and are not necessary to a Federal credit union's business:

(i) the age or location of the dwelling;

(ii) the age or location of dwellings in the neighborhood of the dwelling;

(iii) the income level of the residents in the neighborhood of the dwelling.

(4) Notwithstanding paragraph (c)(3) of this section, it is recognized that there may be factors concerning location of the dwelling which can be properly considered in an appraisal. If any such factor(s) is relied upon, it must be specifically documented in the appraisal, accompanied by a brief statement demonstrating the necessity of using such factor(s). Guidelines

concerning the consideration of location factors appear in paragraph (e)(3) of this section.

(5) Each Federal credit union shall make available, to any requesting member/applicant, a copy of the appraisal used in connection with that member's real estate-related loan application. The appraisal shall be available for a period of 25 months after the applicant has received notice from the Federal credit union of the action taken by the Federal credit union on the real estate-related loan application.

(d) *Nondiscrimination in Advertising:*

(1) *Advertising notice of nondiscrimination compliance.*

(i) No Federal credit union may directly or indirectly engage in any form of advertising of real estate-related loans which implies or suggests that the Federal credit union discriminates in violation of the provisions of the Fair Housing Act or of this section. Advertisements of such loans shall include a facsimile of the following:

We Do Business in Accordance With the Federal Fair Housing Law and the Equal Credit Opportunity Act

(ii) Advertisements of real estate-related loans which are broadcast on the radio shall contain the following statement: "The (insert name) Federal Credit Union is an equal housing lender."

(2) *Lobby notice of nondiscrimination compliance.* Every Federal credit union which engages in real estate-related lending shall conspicuously display in the public lobby of such credit union and in the public area of each office where such loans are made, in a manner so as to be clearly visible to the general public entering such lobby or area, a notice that incorporates a facsimile of the logotype and notice appearing in paragraph (d)(3) of this section. Posters containing this notice and logotype may be obtained from the Regional Offices of the National Credit Union Administration.

(3) *Logotype and notice of nondiscrimination compliance.* The logotype and text of the notice required in paragraph (d)(2) of this section shall be as follows:

We Do Business in Accordance With the Federal Fair Lending Laws

UNDER THE FEDERAL FAIR HOUSING ACT, IT IS ILLEGAL, ON THE BASIS OF RACE, COLOR, NATIONAL ORIGIN, RELIGION, SEX, HANDICAP, OR FAMILIAL STATUS (HAVING CHILDREN UNDER THE AGE OF 18), TO:

- Deny a loan for the purpose of purchasing, constructing, improving, repairing or maintaining a dwelling, or deny any loan secured by a dwelling; or
- Discrimination in fixing the amount, interest rate, duration, application procedures or other terms or conditions of such a loan, or in appraising property.

IF YOU BELIEVE YOU HAVE BEEN DISCRIMINATED AGAINST, YOU SHOULD SEND A COMPLAINT TO:

Assistant Secretary for Fair Housing and Equal Opportunity
Department of Housing & Urban Development
Washington, D.C. 20410
For processing under the Federal Fair Housing Act
and to:
National Credit Union Administration
Office of Examination and Insurance
1775 Duke Street
Alexandria, VA 22314–3428
For processing under NCUA Regulations

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UNDER THE EQUAL CREDIT OPPORTUNITY ACT, IT IS ILLEGAL TO DISCRIMINATE IN ANY CREDIT TRANSACTION:

- On the basis of race, color, national origin, religion, sex, marital status, or age
- Because income is from public assistance, or
- Because a right was exercised under the Consumer Credit Protection Act.

IF YOU BELIEVE YOU HAVE BEEN DISCRIMINATED AGAINST, YOU SHOULD SEND A COMPLAINT TO:

National Credit Union Administration
Office of Examination and Insurance
1775 Duke Street
Alexandria, VA 22314–3428

(e) *Guidelines:*

(1) Compliance with the Fair Housing Act is achieved when each loan applicant's creditworthiness is evaluated on an individual basis, without presuming that the applicant has certain characteristics of a group. If certain lending policies or procedures do presume group characteristics, they may violate the Fair Housing Act, even though the characteristics are not based upon race, color, sex, national origin, religion, handicap, or familial status. Such a violation occurs when otherwise facially nondiscriminatory lending procedures (either general lending policies or specific criteria used in reviewing loan applications) have the effect of making real estate-related loans unavailable or less available on the basis of race, color, sex, national origin, religion, handicap, or familial status. Note, however, that a policy or criterion which has a discriminatory effect is not a violation of

the Fair Housing Act if its use achieves a legitimate business necessity which cannot be achieved by using less discriminatory standards. It is also important to note that the Equal Credit Opportunity Act and Regulation B prohibit discrimination, either per se or in effect, on the basis of the applicant's age, marital status, receipt of public assistance, or the exercise of any rights under the Consumer Credit Protection Act.

(2) Paragraph (b)(3) of this section prohibits consideration of certain factors because of their likely discriminatory effect and because they are not necessary to make sound real estate-related loans. For purposes of clarification, the prohibited use of location factors in this section is intended to prevent abandonment of areas in which a Federal credit union's members live or want to live. It is not intended to require loans in those areas that are geographically remote from the FCU's main or branch offices or that contravene the parameters of a Federal credit union's charter. Further. this prohibition does not preclude requiring a borrower to obtain flood insurance protection pursuant to the National Flood Insurance Act and Part 760 of NCUA's Rules and Regulations, nor does it preclude involvement with Federal or state housing insurance programs which provide for lower interest rates for the purchase of homes in certain urban or rural areas. Also, the legitimate use of location factors in an appraisal does not constitute a violation of the provision of paragraph (b)(3) of this section, which prohibits consideration of location of the dwelling. Finally, the prohibited use of prior home ownership does not preclude a Federal credit union from considering an applicant's payment history on a loan which was made to obtain a home. Such action entails consideration of the payment record on a previous loan in determining creditworthiness; it does not entail consideration of prior home ownership.

(3)(i) Paragraph (c)(3) of this section prohibits consideration of the age or location of a dwelling in a real estate-related loan appraisal. These restrictions are intended to prohibit the use of unfounded or unsubstantiated assumptions regarding the effect upon loan risk of the age of a dwelling or the physical or economic characteristics of an area. Appraisals should be based on the present market value of the property offered as security (including consideration of specific improvements to be made by the borrower) and the likelihood that the property will retain an adequate value over the term of the loan.

(ii) The term "age of the dwelling" does not encompass structural soundness. In addition, the age of the dwelling may be used by an appraiser as a basis for conducting further inspections of certain structural aspects of the dwelling. Paragraph (c)(3) of this section does, however, prohibit an unsubstantiated determination that a house over X years in age is not structurally sound.

(iii) With respect to location factors, paragraph (c)(4) of this section recognizes that there may be location factors which may be considered in an appraisal, and requires that the use of any such factors be specifically documented in the appraisal. These factors will most often be those location factors which may negatively affect the short range future value (up to 3–5 years) of a property. Factors which in some cases may cause the market value of a property to decline are recent zoning changes or a significant number of abandoned homes in the immediate vicinity of the property. However, not all zoning changes will cause a decline in property values, and proximity to abandoned buildings may not affect the market value of a property because the cause of abandonment is unrelated to high risk. Proper considerations include the condition and utility of the improvement and various physical factors such as street conditions, amenities such as parks and recreation areas, availability of public utilities and municipal services and exposure to flooding and land faults.

§ 701.32 Payment on shares by public units and nonmembers.

(a) *Authority.* A Federal credit union may, to the extent permitted under Section 107(6) of the Act and this section, receive payments on shares, (regular shares, share certificates, and share draft accounts) from public units and political subdivisions thereof (as those terms are defined in § 745.1) and nonmember credit unions, and to the extent permitted under the Act, this section and § 701.34, receive payments on shares (regular shares, share certificates, and share draft accounts) from other nonmembers.

(b) *Limitations.* (1) Unless a greater amount has been approved by the Regional Director, the maximum amount of all public unit and nonmember shares shall not, at any given time, exceed 20%

of the total shares of the federal credit union or $1.5 million, whichever is greater.

(2) Before accepting any public unit or nonmember shares in excess of 20% of total shares, the board of directors must adopt a specific written plan concerning the intended use of these shares and forward a copy of the plan to the Regional Director. The plan must include:

(i) A statement of the credit union's needs, sources and intended uses of public unit and nonmember shares;

(ii) Provision for matching maturities of public unit and nonmember shares with corresponding assets, or justification for any mismatch; and

(iii) Provision for adequate income spread between public unit and nonmember shares and corresponding assets.

(3) A federal credit union seeking an exemption from the limits of paragraph (b)(1) of this section must submit to the Regional Director a written request including:

(i) The new maximum level of public unit and nonmember shares requested, either as a dollar amount or a percentage of total shares;

(ii) The current plan adopted by the credit union's board of directors concerning the use of new public unit and nonmember shares;

(iii) A copy of the credit union's latest financial statement; and

(iv) A copy of the credit union's loan and investment policies.

(4) Where the financial condition and management of the credit union are sound and the credit union's plan for the funds is reasonable, there will be a presumption in favor of granting the request. When granted, exemptions will normally be for a two-year period. The Regional Director will provide a written explanation for an exemption that is granted for a lesser time period.

(5) The Regional Director will provide a written determination on an exemption request within 30 calendar days after receipt of the request. The 30-day period will not begin to run until all necessary information has been submitted to the Regional Director. All denials may be appealed to the NCUA Board in a timely manner. Appeals should be submitted through the Regional Director.

(6) Upon expiration of an exemption, nonmember shares currently in the credit union in excess of the limits established pursuant to (b)(1) of this section will continue to be insured by the National Credit Union Insurance Fund within applicable limits. No new shares in excess of the limits established pursuant to (b)(1) of this section shall be accepted. Existing share certificates in excess of the limits established pursuant to (b)(1) of this section may remain in the credit union only until maturity.

(c) The limitations herein do not apply to accounts maintained in accordance with 701.37 (Treasury Tax and Loan Depositaries; Depositaries and Financial Agents of the Government) and matching funds required by 705.7(b) (Community Development Revolving Loan Program for Credit Unions). Once a loan granted pursuant to Part 705 is repaid, nonmember share deposits accepted to meet the matching requirement are subject to this section.

§ 701.33 Reimbursement, Insurance, and Indemnification of Officials and Employees.

(a) *Official.* An "official" is a person who is or was a member of the board of directors, credit committee or supervisory committee, or other volunteer committee established by the board of directors.

(b) *Compensation.*

(1) Only one board officer, if any, may be compensated as an officer of the board. The bylaws must specify the officer to be compensated, if any, as well as the specific duties of each of the board officers. No other official may receive compensation for performing the duties or responsibilities of the board or committee position to which the person has been elected or appointed.

(2) For purposes of this section, the term "compensation" specifically excludes:

(i) payment (by reimbursement to an official or direct credit union payment to a third party) for reasonable and proper costs incurred by an official in carrying out the responsibilities of the position to which that person has been elected or appointed, if the payment is determined by the board of directors to be necessary or appropriate in order to carry out the official business of the credit union, and is in accordance with written policies and procedures, including documentation requirements, established by the board of directors. Such payments may include the payment of travel costs for officials and one immediate family member per official;

(ii) provision of reasonable health, accident and related types of personal insurance

protection, supplied for officials at the expense of the credit union: *Provided,* that such insurance protection must exclude life insurance; must be limited to areas of risk, including accidental death and dismemberment, to which the official is exposed by reason of carrying out the duties or responsibilities of the official's credit union position; must cease immediately upon the insured person's leaving office, without providing residual benefits other than from pending claims, if any; and

(iii) indemnification and related insurance consistent with paragraph (c) of this Section.

(c) *Indemnification.*

(1) A Federal credit union may indemnify its officials and current and former employees for expenses reasonably incurred in connection with judicial or administrative proceedings to which they are or may become parties by reason of the performance of their official duties.

(2) Indemnification shall be consistent either with the standards applicable to credit unions generally in the state in which the principal or home office of the credit union is located, or with the relevant provisions of the Model Business Corporation Act. A Federal credit union that elects to provide indemnification shall specify whether it will follow the relevant state law or the Model Business Corporation Act. Indemnification and the method of indemnification may be provided for by charter or bylaw amendment, contract or board resolution, consistent with the procedural requirements of the applicable state law or the Model Business Corporation Act, as specified. A charter or bylaw amendment must be approved by the National Credit Union Administration.

(3) A Federal credit union may purchase and maintain insurance on behalf of its officials and employees against any liability asserted against them and expenses incurred by them in their official capacities and arising out of the performance of their official duties to the extent such insurance is permitted by the applicable state law or the Model Business Corporation Act.

§ 701.34 Designation of low-income status; receipt of secondary capital accounts by low-income designated credit unions.

(a) *Designation of low-income status.* (1) Section 107(6) of the Federal Credit Union Act (12 U.S.C. 1757(6)) authorizes federal credit unions serving predominantly low-income members to receive shares, share drafts and share certificates from nonmembers. In order to utilize this authority, a federal credit union must receive a low-income designation from its Regional Director. The designation may be removed by the Regional Director upon notice to the federal credit union if the definitions set forth in paragraphs (a) (2) and (3) of this section are no longer met. Removals may be appealed to the NCUA Board within 60 days. Appeals should be submitted through the Regional Director.

(2) The term "low-income members" shall mean those members who make less than 80 percent of the average for all wage earners as established by the Bureau of Labor Statistics or those members whose annual household income falls at or below 80 percent of the median household income for the nation as established by the Census Bureau or those members otherwise defined as low-income members as determined by order of the NCUA Board.

(i) In documenting its low-income membership, a credit union that serves a geographic area where a majority of residents fall at or below the annual income standard is presumed to be serving predominantly low-income members. In applying the standards, Regional Directors shall make allowances for geographical areas with higher costs of living. The following is the exclusive list of geographic areas with the differentials to be used:

	Percent
Hawaii	40
Alaska	36
Washington, DC	19
Boston	17
San Diego	15
Los Angeles	14
New York	13
San Francisco	13
Seattle	10
Chicago	7
Philadelphia	7

(ii) The term "low-income member" also includes those members who are enrolled as full-time or part-time students in a college, university, high school, or vocational school.

(3) The term "predominantly" is defined as a simple majority.

(b) *Receipt of secondary capital accounts by low-income designated credit unions.* A Federal credit union having a designation of low income status pursuant to paragraph (a) of this section may offer secondary capital accounts to nonnatural person

members and nonnatural person nonmembers on the following conditions:

(1) Prior to offering secondary capital accounts, the credit union shall adopt, and forward to the appropriate NCUA Regional Director, a written plan for use of the funds in the secondary capital accounts and subsequent liquidity needs to meet repayment requirements upon maturity of the accounts.

(2) The secondary capital account must be established as a uninsured secondary capital account or other form of non-share account.

(3) The maturity of the secondary capital account must be for a minimum of five years.

(4) The secondary capital account must not be redeemable prior to maturity.

(5) The secondary capital account shall not be insured by the National Credit Union Share Insurance Fund or any governmental or private entity.

(6) The secondary capital account holder's claim against the credit union must be subordinate to all other claims including those of shareholders, creditors and the National Credit Union Share Insurance Fund.

(7) Funds in the secondary capital account (including both principal and interest) must be available to cover operating losses realized by the credit union that exceed its net available reserves and undivided earnings (i.e., reserves and undivided earnings exclusive of allowance accounts for loan and investment losses), and to the extent funds are so used, the credit union shall under no circumstances restore or replenish the account. Losses shall be distributed pro-rata among all secondary capital accounts held by the credit union at the time the losses are realized.

(8) The secondary capital account may not be pledged or provided by the account-holder as security on a loan or other obligation with the credit union or any other party.

(9) In the event of merger or other voluntary dissolution of the credit union, other than merger into another low-income designated credit union, the secondary capital accounts will, to the extent they are not needed to cover losses at the time of merger or dissolution, be closed and paid out to the account-holder.

(10) A secondary capital account contract agreement must be executed between an authorized representative of the account holder and the credit union accurately establishing the terms and conditions of this section and containing no provisions inconsistent therewith.

(11) A disclosure and acknowledgment as set forth in the Appendix to this section must be provided to and executed by an authorized representative of the secondary capital account holder at the time of entering into the account agreement, and original copies of the account agreement and the disclosure and acknowledgment must be retained by the credit union for the term of the agreement.

(c) *Accounting treatment; weighted value for purposes of recognizing capital value of secondary capital accounts.* (1) A low-income designated credit union that issues secondary capital accounts pursuant to paragraph (b) of this section shall record the funds on its balance sheet in an equity account entitled "uninsured secondary capital account." For such accounts with remaining maturities of less than five years, the credit union shall reflect the capital value of the accounts in its financial statement in accordance with the following scale:

(i) Four to less than five years remaining maturity—80 percent.

(ii) Three to less than four years remaining maturity—60 percent.

(iii) Two to less than three years remaining maturity—40 percent.

(iv) One to less than two years remaining maturity—20 percent.

(v) Less than one year remaining maturity—0 percent.

(2) The credit union will reflect the full amount of the secondary capital on deposit in a footnote to its financial statement.

Appendix to § 701.34

Disclosures and acknowledgment in the following form must be provided to any investor in secondary capital accounts in a low-income designated credit union.

An original, signed copy must be retained by the credit union.

Disclosure and Acknowledgment

I, _____ (name of signatory), hereby acknowledge and agree to the following in my capacity as _____ (official position or title) of _____ (name of institutional investor:

• _____ (name of institutional investor) has committed _____ (amount of funds) to a secondary capital account with _____ (name of credit union).

• The funds committed to the secondary capital account are committed for a period of ____ years and are not redeemable prior to _____.

• The secondary capital account is not a share account and the funds committed to the secondary capital account are not insured by the National Credit Union Share Insurance Fund or any other governmental or private entity.

The funds committed to the secondary capital account and any interest paid to the account may be used by _____ (name of credit union) to cover any and all operating losses that exceed the credit union's net available reserves and undivided earnings exclusive of allowance accounts for loan and investment losses), and in the event the funds are so used _____ (name of credit union) will be under no circumstances restore or replenish those funds to _____ (organization).

• In the event of liquidation of _____ (name of credit union), the funds committed to the secondary capital account shall be *subordinate to all other claims* on the assets of the credit union, including claims of member shareholders, creditors and the National Credit Union Share Insurance Fund.

_____

(Signature)

_____

(Official Title)

§ 701.35 Share, Share Draft, and Share Certificate Accounts.

(a) Federal credit unions may offer share, share draft, and share certificate accounts in accordance with Section 107(6) of the Act (12 U.S.C. § 1757(6)) and the board of directors may declare dividends on such accounts as provided in Section 117 of the Act (12 U.S.C. § 1763).

(b) A Federal credit union shall accurately represent the terms and conditions of its share, share draft, and share certificate accounts in all advertising, disclosures, or agreements, whether written or oral.

(c) A federal credit union may, consistent with this section, parts 707 and 740 of this subchapter, other federal law, and its contractual obligations, determine the types of fees or charges and other matters affecting the opening maintaining and closing of a share, share draft or share certificate account. State laws regulating such activities are not applicable to federal credit unions.

(d) For purposes of this Section, "state law" means the constitution, statutes, regulations, and judicial decisions of any state, the District of Columbia, the several territories and possessions of the United States, and the Commonwealth of Puerto Rico.

§ 701.36 FCU Ownership of Fixed Assets.

(a) *A Federal credit union's ownership in fixed assets shall be limited as described in this chapter.*

(b) *Definitions*—As Used in This Section:

(1) Premises includes any office, branch office, suboffice, service center, parking lot, other facility, or real estate where the credit union transacts or will transact business.

(2) Furniture, Fixtures, and Equipment includes all office furnishings, office machines, computer hardware and software, automated terminals, heating and cooling equipment.

(3) Fixed Assets means premises and furniture, fixtures and equipment as these terms are defined above.

(4) Investments in fixed assets means:

(i) any investment in real property (improved or unimproved) which is being used or is intended to be used as premises;

(ii) any leasehold improvement on premises;

(iii) the aggregate of all capital and operating lease payments pursuant to lease agreements for fixed assets;

(iv) any investment in the bonds, stock, debentures, or other obligations of a partnership or corporation, including any entity described in part 712 holding any fixed assets used by the Federal credit union and any loans to such partnership or corporation; or

(v) any investment in furniture, fixtures and equipment.

(5) Abandoned premises means former Federal credit union premises from the date of relocation to new quarters, and property originally acquired for future expansion for which such use is no longer contemplated.

(6) Immediate family member means a spouse or other family members living in the same household.

(7) Shares mean all savings (regular shares, share drafts, share certificates, other savings) and retained earnings means regular reserve,

reserve for contingencies, supplemental reserves, reserve for losses and undivided earnings.

(8) Senior management employee means the credit union's chief executive officer (typically this individual holds the title of President or Treasurer/Manager), any assistant chief executive officers (e.g., Assistant President, Vice President or Assistant Treasurer/Manager) and the chief financial officer (Comptroller).

(c) *Investment in Fixed Assets.*

(1) No Federal credit union with $1,000,000 or more in assets, without the prior approval of the Administration, shall invest in fixed assets if the aggregate of all such investments exceeds 5 percent of shares and retained earnings.

(2) A Federal credit union shall submit such statement and reports as the NCUA regional director may require in support of any investment in fixed assets in excess of the limit specified above.

(3) If the Administration determines that the proposal will not adversely affect the credit union, an aggregate dollar amount or percentage of assets will be approved for investment in fixed assets. Once such a limit has been approved, and unless otherwise specified by the regional director, a Federal credit union may make future acquisitions of fixed assets, provided the aggregate of all such future investments in fixed assets does not exceed an additional 1 percent of the shares and retained earnings of the credit union over the amount approved.

(4) Federal credit unions shall submit their requests to the NCUA regional office having jurisdiction over the geographical area in which the credit union's main office is located. The regional office shall inform the requesting credit union, in writing, of the date the request was received. If the credit union does not receive notification of the action taken on its request within 45 calendar days of the date the request was received by the regional office, the credit union may proceed with its proposed investment in fixed assets.

(d) *Premises.*

(1) When real property is acquired for future expansion, at least partial utilization should be accomplished within a reasonable period, which shall not exceed 3 years unless otherwise approved in writing by the Administration. After real property acquired for future expansion has been held for 1 year, a board resolution with definitive plans for utilization must be available for inspection by an NCUA examiner.

(2) A Federal credit union shall endeavor to dispose of "abandoned premises" at a price sufficient to reimburse the Federal credit union for its investment and costs of acquisition. Current documents must be maintained reflecting the Federal credit union's continuing and diligent efforts to dispose of "abandoned premises." After "abandoned premises" have been on the Federal credit union's books for 4 years, the property must be publicly advertised for sale. Disposition must occur through public or private sale within 5 years of abandonment, unless otherwise approved in writing by the Administration.

(e) *Prohibited Transactions.*

(1) With the exception of a short-term informal lease agreement (maturity less than 1 year) no Federal credit union may acquire or lease premises without the prior written approval of the Administration from any of the following:

(i) a director, member of the credit committee or supervisory committee, or senior management employee of the Federal credit union, or im-mediate family member of any such individual.

(ii) a corporation in which any director, member of the credit committee or supervisory committee, official, or senior management employee, or immediate family members of any such individual, is an officer or director, or has a stock interest of 10 percent or more.

(iii) a partnership in which any director, member of the credit committee or supervisory committee, or senior management employee, or immediate family members of any such individual, is a general partner, or a limited partner with an interest of 10 percent or more.

(2) The prohibition contained in paragraph (e)(1) also applies to any employee not otherwise covered if the employee is directly involved in investments in fixed assets unless the board of directors determines that the employee's involvement does not present a conflict of interest.

(3) All transactions with business associates or family members not specifically prohibited by this subsection (e) must be conducted at arm's length and in the interest of the credit union.

§ 701.37 Treasury Tax and Loan Depositaries; Depositaries and Financial Agents of the Government.

(a) *Definitions.*

(1) "Treasury Tax and Loan ("TT&L") Remittance Account" means a nondividend-paying account, the balance of which is subject to the right of immediate withdrawal, established for receipt of payments of Federal taxes and certain United States obligations under United States Treasury Department regulations.

(2) "TT&L Note Account" means an account subject to the right of immediate call, evidencing funds held by depositaries electing the note option under United States Treasury Department regulations.

(3) "Treasury General Account" means an account, established under United States Treasury Department regulations, in which a zero balance may be maintained and from which the entire balance may be withdrawn by the depositor immediately under all circumstances except closure of the credit union;

(4) "U.S. Treasury Time Deposit-Open Account" means a nondividend-bearing account, established under United States Treasury Department regulations, which generally may not be withdrawn until the expiration of 14 days after the date of the United States Treasury Department's written notice of intent to withdraw.

(b) Subject to regulation of the United States Treasury Department, a Federal credit union may serve as a Treasury tax and loan depositary, a depositary of Federal taxes, a depositary of public money, and a financial agent of the United States Government. In serving in these capacities, a Federal credit union may maintain the accounts defined in subsection (a), pledge collateral, and perform the services described under United States Treasury Department regulations for institutions acting in these capacities.

(c) Funds held in a TT&L Remittance Account, a TT&L Note Account, a Treasury General Account, and a U.S. Treasury Time Deposit-Open Account shall be considered deposits of public funds. Funds held in a TT&L Remittance Account and a TT&L Note Account shall be added together and insured up to a maximum of $100,000 in the aggregate. Funds held in a Treasury General Account and a U.S. Treasury Time Deposit-Open Account shall be added together and insured up to a maximum of $100,000 in the aggregate.

(d) Funds held in a TT&L Remittance Account, a TT&L Note Account, a Treasury General Account, and U.S. Treasury Time Deposit-Open Account are not subject to the 60-day notice requirement of Article III, section 5(a) of the Federal Credit Union Bylaws.

§ 701.38 Borrowed Funds From Natural Persons.

(a) Federal credit unions may borrow from a natural person, PROVIDED:

(1) The borrowing is evidenced by a signed promissory note which sets forth the terms and conditions regarding maturity, prepayment, interest rate, method of computation, and method of payment;

(2) The promissory note and any advertisement for such funds contains conspicuous language indicating that:

(i) the note represents money borrowed by the credit union;

(ii) the note does not represent shares and, therefore, is not insured by the National Credit Union Share Insurance Fund.

in a form that the member or potential member may keep. Disclosures for each account offered by a credit union may be presented separately or they may be combined with disclosures for the credit union's other accounts, as long as it is clear which disclosures are applicable to the member's account.

(b) *General.* The disclosures shall reflect the terms of the legal obligation between the member and the credit union. Disclosures may be made in languages other than English, provided the disclosures are available in English upon request.

(c) *Relation to Regulation E (12 CFR part 205).* Disclosures required by and provided in accordance with the Electronic Fund Transfer Act (15 U.S.C. 1601) and its implementing Regulation E (12 CFR part 205) that are also required by this part may be substituted for the disclosures required by this part.

(d) *Multiple members.* If an account is held by more than one member, disclosures may be made to any one of the members.

(e) *Oral responses to inquiries.* In an oral response to a member or potential member's inquiry about dividend rates payable on its accounts, the credit union shall state the annual percentage yield. The dividend rate may be stated in addition to the annual percentage yield. No other rate may be stated. In stating a dividend rate and annual percentage yield, a credit union shall:

(1) For dividend-bearing accounts other than term share accounts, specify a dividend rate and annual percentage yield as of the last dividend declaration date. In the event that disclosures of a dividend rate and annual percentage yield as of the last dividend declaration date might be inaccurate because of known or contemplated dividend rate changes, the credit union may disclose the prospective dividend rate and prospective annual percentage yield. Such prospective dividend rate and prospective annual percentage yield may be disclosed either in lieu of, or in addition to, the dividend rate and annual percentage yield as of the last dividend declaration date.

(2) For interest-bearing accounts and for dividend-bearing term share accounts, specify an interest (dividend) rate and annual percentage yield that were offered within the most recent seven calendar days; state that the rate and yield are accurate as of an identified date; and provide a telephone number members may call to obtain current rate information.

(f) *Rounding and accuracy rules for rates and yields.*

(1) *Rounding.* The annual percentage yield, the annual percentage yield earned, and the dividend rate shall be rounded to the nearest one-hundredth of one percentage point (.01%) and expressed to two decimal places. For account disclosures, the dividend rate may be expressed to more than two decimal places.

(2) *Accuracy.* The annual percentage yield (and the annual percentage yield earned) will be considered accurate if not more than one-twentieth of one percentage point (.05%) above or below the annual percentage yield (and the annual percentage yield earned) determined in accordance with the rules in Appendix A of this part.

§ 707.4 Account disclosures.

(a) *Delivery of account disclosures.*

(1) *Account opening.* The credit union shall provide the account disclosures to the member or potential member before an account is opened or a service is provided, whichever is earlier. A credit union is deemed to have provided a service when a fee required to be disclosed is assessed. If the member is not present at the credit union when the account is opened or a service is provided and has not already received the disclosures, the credit union shall mail or deliver the disclosures no later than twenty calendar days after the account is opened or the service is provided, whichever is earlier.

(2) *Requests.*

(i) A credit union shall provide the account disclosures to any member or potential member upon request. A credit union may provide the account disclosures to nonmembers in its sole discretion. If the member is not present at the credit union when the request is made, the credit union shall mail or deliver the disclosures within a reasonable time after it receives the request.

(ii) In providing disclosures upon request, the credit union may:

(A) Specify rates as follows:

(*1*) For dividend-bearing accounts other than term share accounts, specify a dividend rate and annual percentage yield as of the last dividend declaration date. In the event that disclosures of a dividend rate and annual percentage yield as of the last dividend declaration date might be inaccurate because of known or contemplated dividend rate changes, the credit union may disclose the prospective divi-

dend rate and prospective annual percentage yield. Such prospective dividend rate and prospective annual percentage yield may be disclosed either in lieu of, or in addition to, the dividend rate and annual percentage yield as of the last dividend declaration date.

(*2*) For interest-bearing accounts and for dividend-bearing term share accounts, specify an interest rate and annual percentage yield that were offered within the most recent seven calendar days; state that the rate and yield are accurate as of an identified date; and provide a telephone number members may call to obtain current rate information; and

(B) State the maturity of a term share account as either a term or a date.

(b) Content of account disclosures. Account disclosures shall include the following, as applicable:

(1) *Rate information.*

(i) *Annual percentage yield and dividend rate.*

(A) For interest-bearing accounts and for dividend-bearing term share accounts, the "annual percentage yield" and the "interest rate" ("dividend rate"), using those terms, and for fixed-rate accounts the period of time the interest (dividend) rate will be in effect.

(B) For dividend-bearing accounts other than term share accounts, a credit union shall specify a dividend rate and annual percentage yield (using those terms) as of the last dividend declaration date. In the event that disclosures of a dividend rate and annual percentage yield as of the last dividend declaration date might be inaccurate because of known or contemplated dividend rate changes, the credit union may disclose the prospective dividend rate and prospective annual percentage yield. Such prospective dividend rate and prospective annual percentage yield may be disclosed either in lieu of, or in addition to, the dividend rate and annual percentage yield as of the last dividend declaration date.

(ii) *Variable rates.* For variable-rate accounts:

(A) The fact that the dividend rate and annual percentage yield may change;

(B) How the dividend rate is determined;

(C) The frequency with which the dividend rate may change; and

(D) Any limitation on the amount the dividend rate may change.

(2) *Compounding and crediting.*

(i) *Frequency.* The frequency with which dividends are compounded and credited, and the dividend period for dividend-bearing accounts.

(ii) *Effect of closing an account.* If members will forfeit dividends if they close an account before accrued dividends are credited, a statement that the dividends will not be paid in such cases.

(3) *Balance information.*

(i) *Minimum balance requirements.* Any minimum balance required to:

(A) Open the account;

(B) Avoid the imposition of a fee; or

(C) Obtain the annual percentage yield disclosed.

Except for the balance to open the account, the disclosure shall state how the balance is determined for these purposes.

(ii) *Balance computation method.* An explanation of the balance computation method specified in § 707.7, used to calculate dividends on the account.

(iii) *When dividends begin to accrue.* A statement of when dividends begin to accrue on noncash deposits.

(4) *Fees.* The amount of any fee that may be imposed in connection with the account (or an explanation of how the fee will be determined) and the conditions under which the fee may be imposed.

(5) *Transaction limitations.* Any limitations on the number or dollar amount of withdrawals or deposits.

(6) *Features of Term Share Accounts.* For term share accounts:

(i) *Time requirements.* The maturity date.

(ii) *Early withdrawal penalties.* A statement that a penalty will be imposed for early withdrawal, how it is calculated, and the conditions for its assessment.

(iii) *Withdrawal of dividends prior to maturity.* If compounding occurs and dividends may be withdrawn prior to maturity, a statement that the annual percentage yield assumes dividends remain in the account until maturity and that a withdrawal will reduce earnings. For accounts with a stated maturity greater than one year that do not compound dividends on an annual or more frequent basis, that require dividend payouts at least annually, and that disclose an APY determined in accordance with section E of appendix A of this part, a statement that dividends cannot remain on account and that payout of dividends is mandatory.

(iv) *Renewal policies.* A statement of whether or not the account will renew automatically at maturity. If it will, a statement of whether or not a grace period will be provided and, if so, the length of that period must be stated. If the account will not renew automatically, a statement of whether dividends will be paid after maturity if the member does not renew the account must be stated.

(7) *Bonuses.* The amount or type of any bonus, when the bonus will be provided, and any minimum balance and time requirements to obtain the bonus.

(8) *Nature of dividends.* For accounts earning dividends, other than term share accounts, a statement that dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

(c) *Notice to existing account holders.*

(1) *Notice of availability of disclosures.* Credit unions shall provide a notice to members who receive periodic statements and who hold existing accounts of the type offered by the credit union on January 1, 1995. The notice shall be included on or with the first periodic statement sent after January 1, 1995 (or on or with the first periodic statement for a statement cycle beginning on or after that date). The notice shall state that the members may request account disclosures containing terms, fees, and rate information for the account. In responding to such a request, credit unions shall provide disclosures in accordance with paragraph (a)(2) of this section.

(2) *Alternative to notice.* As an alternative to the notice described in paragraph (c)(1) of this section, credit unions may provide account disclosures to members. The disclosures may be provided either with a periodic statement or separately, but must be sent no later than when the periodic statement described in paragraph (c)(1) of this section is sent.

§ 707.5 Subsequent disclosures.

(a) *Change in terms.*

(1) *Advance notice required.* A credit union shall give advance notice to affected members of any change in a term required to be disclosed under § 707.4(b), if the change may reduce the annual percentage yield or adversely affect the member. The notice shall include the effective date of the change. The notice shall be mailed or delivered at least 30 calendar days before the effective date of the change.

(2) *No notice required.* No notice under this section is required for:

(i) *Variable-rate changes.* Changes in the dividend rate and corresponding changes in the annual percentage yield in variable-rate accounts.

(ii) *Share draft and check printing fees.* Changes in fees for check printing.

(iii) *Short-term term share accounts.* Changes in any term for term share accounts with maturities of one month or less.

(b) *Notice before maturity for term share accounts longer than one month that renew automatically.* For term share accounts with a maturity longer than one month that renew automatically at maturity, credit unions shall provide the disclosures described below before maturity. The disclosures shall be mailed or delivered at least 30 calendar days before maturity of the existing account. Alternatively, the disclosures may be mailed or delivered at least 20 calendar days before the end of the grace period on the existing account, provided a grace period of at least five calendar days is allowed.

(1) *Maturities of longer than one year.* If the maturity is longer than one year, the credit union shall provide account disclosures set forth in § 707.4(b) for the new account, along with the date the existing account matures. If the dividend rate and annual percentage yield that will be paid for the new account are unknown when disclosures are provided, the credit union shall state that those rates have not yet been determined, the date when they will be determined, and a telephone number members may call to obtain the dividend rate and the annual percentage yield that will be paid for the new account.

(2) *Maturities of one year or less but longer than one month.* If the maturity is one year or less but longer than one month, the credit union shall either:

(i) Provide disclosures as set forth in paragraph (b)(1) of this section; or

(ii) Disclose to the member:

(A) The date the existing account matures and the new maturity date if the account is renewed;

(B) The dividend rate and the annual percentage yield for the new account if they are known (or that those rates have not yet been determined, the date when they will be determined, and a telephone number the member

may call to obtain the dividend rate and the annual percentage yield that will be paid for the new account); and

(C) Any difference in the terms of the new account as compared to the terms required to be disclosed under § 707.4(b) for the existing account.

(c) *Notice before maturity for term share accounts longer than one year that do not renew automatically.* For term share accounts with a maturity longer than one year that do not renew automatically at maturity, credit unions shall disclose to members the maturity date and whether dividends will be paid after maturity. The disclosures shall be mailed or delivered at least 10 calendar days before maturity of the existing account.

§ 707.6 Statement disclosures.

(a) *Rule when statement and crediting periods vary.* In making the disclosures described in paragraph (b) of this section, credit unions that calculate and credit dividends for a period other than the statement period, such as the dividend period, may calculate and disclose the annual percentage yield earned and amount of dividends earned based on that period rather than the statement period. The information in paragraph (b)(4) shall be stated for that period as well as for the statement period.

(b) *Statement disclosures.* If a credit union mails or delivers a periodic statement, the statement shall include the following disclosures:

(1) *Annual percentage yield earned.* The "annual percentage yield earned," using that term as calculated according to the rules in Appendix A of this part.

(2) *Amount of dividends.* The dollar amount of dividends earned (accrued or paid and credited) on the account. The dollar amount of any extraordinary dividends earned during the statement period shall be shown as a separate figure.

(3) *Fees imposed.* Fees required to be disclosed under § 707.4(b)(4) of this part and imposed on the account during the statement period. The fees shall be itemized by type and dollar amounts.

(4) *Length of period.* The total number of days in the statement period, or the beginning and ending dates of the period.

§ 707.7 Payment of dividends.

(a) *Permissible methods.*

(1) *Balance on which dividends are calculated.* Credit unions shall calculate dividends on the full amount of principal in an account for each day by use of either the daily balance method or the average daily balance method. Credit unions shall calculate dividends by use of a daily rate of at least 1/365 of the dividend rate. In a leap year a daily rate of 1/366 of the dividend rate may be used.

(2) *Determination of minimum balance to earn dividends.* A credit union shall use the same method to determine any minimum balance required to earn dividends as it uses to determine the balance on which dividends are calculated. A credit union may use an additional method that is unequivocally beneficial to the member.

(b) *Compounding and crediting policies.* This section does not require credit unions to compound or credit dividends at any particular frequency.

(c) *Date dividends begin to accrue.* Dividends shall begin to accrue not later than the day specified in § 606 of the Expedited Funds Availability Act (12 U.S.C. 4005) and implementing Regulation CC (12 CFR part 229). Dividends shall accrue on funds until the day funds are withdrawn.

§ 707.8 Advertising.

(a) *Misleading or inaccurate advertisements.* An advertisement shall not be misleading or inaccurate and shall not misrepresent a credit union's account contract. An advertisement shall not refer to or describe an account as "free" or "no cost" (or contain a similar term) if any maintenance or activity fee may be imposed on the account. The word "profit" shall not be used in referring to interest paid on an account.

(b) *Permissible rates.* If an advertisement states a rate of return, it shall state the rate as an "annual percentage yield," using that term. (The abbreviation "APY" may be used provided the term "annual percentage yield" is stated at least once in the advertisement.) The advertisement shall not state any other rate, except that the "dividend rate," using that term, may be stated in conjunction with, but not more conspicuously than, the annual percentage yield to which it relates.

(c) *When additional disclosures are required.* Except as provided in paragraph (e) of this section,

if the annual percentage yield is stated in an advertisement shall state the following information, to the extent applicable, clearly and conspicuously:

(1) *Variable rates.* For variable-rate accounts, a statement that the rate may change after the account is opened.

(2) *Time annual percentage yield is offered.* For interest-bearing accounts and dividend-bearing term share accounts, the period of time the annual percentage yield will be offered, or a statement that the annual percentage yield is accurate as of a specified date. For dividend-bearing accounts other than term share accounts, a statement that the annual percentage yield is accurate as of the last dividend declaration date. In the event that disclosure of an annual percentage yield as of the last dividend declaration date might be inaccurate because of known or contemplated dividend rate changes, the credit union may disclose the prospective annual percentage yield. Such prospective annual percentage yield may be disclosed either in lieu of, or in addition to, the dividend rate and annual percentage yield as of the last dividend declaration date.

(3) *Minimum balance.* The minimum balance required to earn the advertised annual percentage yield. For tiered-rate accounts, the minimum balance required for each tier shall be stated in close proximity and with equal prominence to the applicable annual percentage yield.

(4) *Minimum opening deposit.* The minimum deposit required to open the account, if it is greater than the minimum balance necessary to earn the advertised annual percentage yield.

(5) *Effect of fees.* A statement that fees could reduce the earnings on the account.

(6) *Features of term share accounts.* For term share accounts:

(i) *Time requirements.* The term of the account.

(ii) *Early withdrawal penalties.* A statement that a penalty will or may be imposed for early withdrawal.

(iii) *Required dividend payouts.* For noncompounding term share accounts with a stated maturity greater than one year that do not compound dividends on an annual or more frequent basis, that require dividend payouts at least annually, and that disclose an APY determined in accordance with section E of appendix A of this part, a statement that dividends cannot remain on account and that payout of dividends is mandatory.

(d) *Bonuses.* Except as provided in paragraph (e) of this section, if a bonus is stated in an advertisement, the advertisement shall state the following information, to the extent applicable, clearly and conspicuously:

(1) The "annual percentage yield," using that term;

(2) The time requirements to obtain the bonus;

(3) The minimum balance required to obtain the bonus;

(4) The minimum balance required to open the account, if it is greater than the minimum balance necessary to obtain the bonus; and

(5) When the bonus will be provided.

(e) *Exemption for certain advertisements.*

(1) *Certain media.* If an advertisement is made through one of the following media, it need not contain the information in paragraphs (c)(1), (c)(2), (c)(4), (c)(5), (c)(6)(ii), (d)(4) and (d)(5) of this section:

(i) Broadcast or electronic media, such as television or radio;

(ii) Outdoor media, such as billboards; or

(iii) Telephone response machines.

(2) *Indoor signs.*

(i) Signs inside the premises of a credit union (or the premises of a share or deposit broker) are not subject to paragraphs (b), (c), (d) or (e)(1) of this section.

(ii) If a sign exempted by paragraph (e)(2) of this section states a rate of return, it shall:

(A) State the rate as an "annual percentage yield," using that term or the term "APY." The sign shall not state any other rate, except that the dividend rate may be stated in conjunction with the annual percentage yield to which it relates.

(B) Contain a statement advising members to contact an employee for further information about applicable fees and terms.

(3) *Newsletters.*

(i) Newsletters sent by a credit union to existing members only are not subject to paragraphs (b), (c), (d) or (e)(1) of this section.

(ii) If a newsletter exempted by paragraph (e)(3) of this section states a rate of return, it shall:

(A) State the rate as an "annual percentage yield," using that term or the term "APY." The newsletter shall not state any other rate, except that the dividend rate may be stated in conjunction with the annual percentage yield to which it relates.

(B) Contain a statement advising members to contact an employee for further information about applicable fees and terms.

§ 707.9 Enforcement and record retention.

(a) *Administrative enforcement.* Section 270 of TISA (12 U.S.C. 4309) contains the provisions relating to administrative sanctions for failure to comply with the requirements of TISA and this part.

(b) *Civil liability.* Section 271 of TISA (12 U.S.C. 4310) contains the provisions relating to civil liability for failure to comply with the requirements of TISA and this part; Section 271 is repealed effective September 30, 2001.

(c) *Record retention.* A credit union shall retain evidence of compliance with this regulation for a minimum of two years after the date disclosures are required to be made or action is required to be taken.

Appendix A to Part 707—Annual Percentage Yield Calculation

The annual percentage yield (APY) measures the total amount of dividends a credit union pays on an account based on the dividend rate and the frequency of compounding. The annual percentage yield is expressed as an annualized rate, based on a 365-day year. (Credit unions may calculate the annual percentage yield based on a 365-day or a 366-day year in a leap year.) Part I of this appendix discusses the annual percentage yield calculations for account disclosures and advertisements, while Part II discusses annual percentage yield earned calculations for statements. The annual percentage yield reflects only dividends and does not include the value of any bonus, as that term is defined in part 707, that may be provided to the member to open, maintain, increase or renew an account. Dividends, interest or other earnings are not to be included in the annual percentage yield if such amounts are determined by circumstances that may or may not occur in the future. These formulas apply to both dividend-bearing and interest-bearing accounts held by credit unions.

Part I. Annual Percentage Yield for Account Disclosures and Advertising Purposes

In general, the annual percentage yield for account disclosures under §§ 707.4 and 707.5 and for advertising under § 707.8 is an annualized rate that reflects the relationship between the amount of dividends that would be earned by the member for the term of the account and the amount of principal used to calculate those dividends. The amount of dividends that would be earned may be projected based on the most recent past declared rate or an anticipated future rate, whichever the credit union judges to most reasonably approximate the dividends to be earned. Special rules apply to accounts with tiered and stepped dividend rates, and to certain term share accounts with a stated maturity greater than one year.

A. General rules

Except as provided in Part I. E. of this appendix, the annual percentage yield shall be calculated by the formula shown below. Credit unions may calculate the annual percentage yield using projected dividends based on either the rate at the last dividend declaration date or the rate anticipated at a future date. The credit union must disclose whichever option it uses to members. Credit unions shall calculate the annual percentage yield based on the actual number of days for the term of the account. For accounts without a stated maturity date (such as a typical share or share draft account), the calculation shall be based on an assumed term of 365 days. In determining the total dividends figure to be used in the formula, credit unions shall assume that all principal and dividends remain on deposit for the entire term, and that no other transactions (deposits or withdrawals) occur during the term. (This assumption shall not be used if a credit union requires, as a condition of the account, that members withdraw dividends during the term. In such a case, the dividends (and annual percentage yield calculation) shall reflect that requirement.) For term share accounts that are offered in multiples of months, credit unions may base the number of days on either the actual number of days during the applicable period, or the number of days that would occur for any actual sequence of that many calendar months. If credit unions choose to use this permissive rule, they must use the same number of days to calculate the dollar amount of dividends that will be earned on the account in the annual percentage yield formula (where "Dividends" are divided by "Principal".)

The annual percentage yield is to be calculated by use of the following general formula (("APY") is used for convenience in the formulas):

$$APY = 100[(1 + Dividends/Principal)^{(365/Days\ in\ term)} - 1]$$

"Principal" is the amount of funds assumed to have been deposited at the beginning of the account.

"Dividends" is the total dollar amount of dividends earned on the Principal for the term of the account.

"Days in term" is the actual number of days in the term of the account.

When the "days in term" is 365 (that is, where the stated maturity is 365 days or where the account does not have a stated maturity), the APY can be calculated by use of the following simple formula:

$$APY = 100\ (Dividends/Principal).$$

EXAMPLES:

(1) If a credit union would pay $61.68 in dividends for a 365-day year on $1,000 deposited into a share draft account, the APY is 6.17%:

$$APY = 100 [(1 + 61.68/1,000)^{(365/365)} - 1]$$

APY = 6.17%

Or, using the simple formula above (since the term is deemed to be 365 days):

APY = 100 (61.68/1,000)

APY = 6.17%

(2) If a credit union pays $30.37 in dividends on a $1,000 six-month term share certificate account (where the six-month period used by the credit union contains 182 days), using the general formula above, the APY is 6.18%:

$$APY = 100 [(1 + 30.37/1,000)^{(365/182)} - 1]$$

APY = 6.18%

The APY is affected by the frequency of compounding, i.e., the amount of dividends will be greater the more frequently dividends are compounded for a given nominal rate. When two credit unions are offering the same dividend rate on, for example, a share account, the APY disclosed may be different if the credit unions use a different frequency of compounding.

EXAMPLES:

(1) If a credit union pays $1,268.25 in dividends for a 365-day year on $10,000 deposited into a regular share account earning 12%, and the dividends are compounded monthly, the APY will be 12.68%:

APY = 100 ($1,268.25/10,000)

APY = 12.68%

(2) However, if a credit union is compounding dividends on a quarterly basis on an account which otherwise has the same terms, the dividends will be $1,255.09 and the APY will be 12.55%:

APY = 100 ($1,255.09/10,000)

APY = 12.55%

B. Stepped-Rate Accounts (Different Rates Apply in Succeeding Periods)

For accounts with two or more dividend rates applied in succeeding periods (where the rates are known at the time the account is opened), a credit union shall assume each dividend rate is in effect for the length of time provided for in any share agreement.

EXAMPLES:

(1) If a credit union offers a $1,000 6-month term share (certificate) account on which it pays a 5% dividend rate, compounded daily, for the first three months (which contain 91 days), and a 5.5% dividend rate, compounded daily, for the next three months (which contain 92 days), the total dividends for six months is $26.68, and, using the general formula above, the APY is 5.39%:

$$APY = 100 [(1 + 26.68/1,000)^{(365/183)} - 1]$$

APY = 5.39%

(2) If a credit union offers a $1,000 2-year share certificate on which it pays a 6% dividend rate, compounded daily, for the first year, and a 6.5% dividend rate, compounded daily, for the next year, the total dividends for two years is $133.13, and, using the general formula above, the APY is 6.45%:

$$APY = 100[(1 + 133.13/1,000)^{(365/730)} - 1]$$

APY = 6.45%

C. Variable-Rate Accounts

For variable-rate accounts without an introductory premium or discounted rate, a credit union must base the calculation only on the initial dividend rate in effect when the account is opened (or advertised), and assume that this rate will not change during the year.

Variable-rate accounts with an introductory premium or discount rate must be treated like stepped-rate accounts. Thus, a credit union shall assume that: (1) the introductory simple dividend rate is in effect for the length of time provided for in the account contract; and (2) the variable dividend rate that would have been in effect when the account is opened or advertised (but for the introductory rate) is in effect for the remainder of the year. If the variable rate is tied to an index, the index-based rate in effect at the time of disclosure must be used for the remainder of the year. If the rate is not tied to an index, the rate in effect for existing members holding the same account (who are not receiving the introductory dividend rate) must be used for the remainder of the year.

For example, if a credit union offers an account on which it pays a 7% dividend rate, com-

pounded daily, for the first three months (which, for example, contains 91 days), while the variable dividend rate that would have been in effect when the account was opened was 5%, the total dividends for a 365-day year for a $1,000 account balance is $56.52, (based on 91 days at 7% followed by 274 days at 5%). Using the simple formula, the APY is 5.65%:

APY = 100 (56.52/1,000)

APY = 5.65%

D. Accounts With Tiered Rates (Different Rates Apply To Specified Balance Level)

For accounts in which two or more dividend rates paid on the account are applicable to specified balance levels, the credit union must calculate the annual percentage yield in accordance with the method described below that it uses to calculate dividends. In all cases, an annual percentage yield (or a range of annual percentage yields, if appropriate) must be disclosed for each balance tier.

For purposes of the examples discussed below, assume the following:

Simple dividend rate	*Share balance required to earn rate*
5.25%	up to but not exceeding $2,500
5.50%	above $2,500, but not exceeding $15,000
5.75%	above $15,000.

Tiering Method A

Under this method, a credit union pays on the full balance in the account the stated dividend rate that corresponds to the applicable share balance tier. For example, if a member deposits $8,000, the credit union pays the 5.50% dividend rate on the entire $8,000. This is also known as a "hybrid" or "plateau" tiered rate account.

When this method is used to determine dividends, only one annual percentage yield will apply to each tier. Within each tier, the annual percentage yield will not vary with the amount of principal assumed to have been deposited.For the dividend rates and account balances assumed above, the credit union will state three annual percentage yields—one corresponding to each balance tier. Calculation of each annual percentage yield is similar for this type of account as for accounts with a single fixed dividend rate. Thus, the calculation is based on the total amount of dividends that would be received by the member for each tier of the account for a year and the principal assumed to have been deposited to earn that amount of dividends.

First tier. Assuming daily compounding, the credit union will pay $53.90 in dividends on a $1,000 account balance. Using the general formula for the first tier, the APY is 5.39%:

$$APY = 100\ [(1 + 53.90/1,000)^{(365/365)} - 1]$$

APY = 5.39%

Using the simple formula:

APY = 100 (53.90/1,000)

APY = 5.39%

Second tier. The credit union will pay $452.29 in dividends on a $8,000 deposit. Thus, using the simple formula, the annual percentage yield for the second tier is 5.65%:

APY = 100 (452.29/8,000)

APY = 5.65%

Third tier. The credit union will pay $1,183.61 in dividends on a $20,000 account balance. Thus, using the simple formula, the annual percentage yield for the third tier is 5.92%:

APY = 100 (1,183.61/20,000)

APY = 5.92%

Tiering Method B

Under this method, a credit union pays the stated dividend rate only on that portion of the balance within the specified tier. For example, if a member deposits $8,000, the credit union pays 5.25% on only $2,500 and 5.50% on $5,500 (the difference between $8,000 and the first tier cutoff of $2,500). This is also known as a "pure" tiered rate account.

The credit union that computes dividends in this manner must provide a range that shows the lowest and the highest annual percentage yields for each tier (other than for the first tier, which, like the tiers in Method A, has the same annual percentage yield throughout). The low figure for an annual percentage yield is calculated based on the total amount of dividends earned for a year assuming the minimum principal required to earn the dividend rate for that tier. The high figure for an annual percentage yield is based on the amount of dividends the credit union would pay on the highest principal

that could be deposited to earn that same dividend rate. If the account does not have a limit on the amount that can be deposited, the credit union may assume any amount.

For the tiering structure assumed above, the credit union would state a total of five annual percentage yields—one figure for the first tier and two figures stated as a range for the other two tiers.

First tier. Assuming daily compounding, the credit union could pay $53.90 in dividends on a $1,000 account balance. For this first tier, using the simple formula, the annual percentage yield is 5.39%:

APY = 100 (53.90/1,000)

APY = 5.39%

Second tier. For the second tier the credit union would pay between $134.75 and $841.45 in dividends, based on assumed balances of $2,500.01 and $15,000, respectively. For $2,500.01, dividends would be figured on $2,500 at 5.25% dividend rate plus dividends on $.01 at 5.50%. For the low end of the second tier, therefore, the annual percentage yield is 5.39%. Using the simple formula:

APY = 100 (134.75/2,500)

APY = 5.39%

For $15,000, dividends are figured on $2,500 at 5.25% dividend rate plus dividends on $12,500 at 5.50% dividend rate. For the high end of the second tier, the annual percentage yield, using the simple formula, is 5.61%:

APY = 100 (841.45/15,000)

APY = 5.61%

Thus, the annual percentage yield range that would be stated for the second tier is 5.39% to 5.61%.

Third tier. For the third tier, the credit union would pay $841.45 and $5,871.78 in dividends on the low end of the third tier (a balance of $15,000.01). For $15,000.01, dividends would be figured on $2,500 at 5.25% dividend rate, plus dividends on $12,500 at 5.50% dividend rate, plus dividends on $.01 at 5.75% dividend rate. For the low end of the third tier, therefore, the annual percentage yield, using the simple formula, is 5.61%:

APY = 100 (841.45/15,000)

APY = 5.61%

Assuming the credit union does not limit the account balance, it may assume any maximum amount for the purposes of computing the annual percentage yield for the high end of the third tier. For an assumed maximum balance amount of $100,000, dividends would be figured on $2,500 at 5.25% dividend rate, plus dividends on $12,500 at 5.50% dividend rate, plus dividends on $85,000 at 5.75% dividend rate. For the high end of the third tier, therefore, the annual percentage yield, using the simple formula, is 5.87%:

APY = 100 (5,871.78/100,000)

APY = 5.87%

Thus, the annual percentage yield that would be stated for the third tier is 5.61% to 5.87%. If the assumed maximum balance amount is $1,000,000, credit unions would use $985,000 rather than $85,000 in the last calculation. In that case for the high end of the third tier, the annual percentage yield, using the simple formula, is 5.91%:

APY = 100 (59,134.22/1,000,000)

APY = 5.91%

Thus, the annual percentage yield range that would be stated for the third tier is 5.61% to 5.91%.

E. Term Share Accounts with a Stated Maturity Greater than One Year that Pay Dividends At Least Annually

1. For term share accounts with a stated maturity greater than one year, that do not compound dividends on an annual or more frequent basis, and that require the member to withdraw dividends at least annually, the annual percentage yield may be disclosed as equal to the dividend rate.

EXAMPLE

If a credit union offers a $1,000 two-year term share account that does not compound and that pays out dividends semi-annually by check or transfer at a 6.00% dividend rate, the annual percentage yield may be disclosed as 6.00%.

2. For term share accounts covered by this paragraph that are also stepped-rate accounts, the annual percentage yield may be disclosed as equal to the composite dividend rate.

EXAMPLE

(1) If a credit union offers a $1,000 three-year term share account that does not compound and

that pays out dividends annually by check or transfer at a 5.00% dividend rate for the first year, 6.00% dividend rate for the second year, and 7.00% dividend rate for the third year, the credit union may compute the composite dividend rate and APY as follows:

(a) Multiply each dividend rate by the number of days it will be in effect;

(b) Add these figures together; and

(c) Divide by the total number of days in the term.

(2) Applied to the example, the products of the dividend rates and days the rates are in effect are (5.00%×365 days) 1825, (6.00%×365 days) 2190, and (7.00%×365) 2555, respectively. The sum of these products, 6570, is divided by 1095, the total number of days in the term. The composite dividend rate and APY are both 6.00%.

Part II. Annual Percentage Yield Earned for Statements

The annual percentage yield earned for statements under § 707.6 is an annualized rate that reflects the relationship between the amount of dividends actually earned (accrued or paid and credited) to the member's account during the period and the average daily balance in the account for the period over which the dividends were earned.

Pursuant to § 707.6(a), when dividends are paid less frequently than statements are sent, the APY Earned may reflect the number of days over which dividends were earned rather than the number of days in the statement period, e.g., if a credit union uses the average daily balance method and calculates dividends for a period other than the statement period, the annual percentage yield earned shall reflect the relationship between the amount of dividends earned and the average daily balance in the account for the other period, such as a crediting or dividend period.

The annual percentage yield shall be calculated by using the following formulas ("APY Earned" is used for convenience in the formulas):

A. General formula

$$\text{APY Earned} = 100[(1 + \text{Dividends earned}/\text{Balance})^{(365/\text{Days in period})} - 1]$$

"Balance" is the average daily balance in the account for the period.

"Dividends earned" is the actual amount of dividends accrued or paid and credited to the account for the period.

"Days in period" is the actual number of days over which the dividends disclosed on the statement were earned.

EXAMPLES:

(1) If a credit union calculates dividends for the statement period (and uses either the daily balance or the average daily balance method), and the account had a balance of $1,500 for 15 days and a balance of $500 for the remaining 15 days of a 30-day statement period, the average daily balance for the period is $1,000. Assume that $5.25 in dividends was earned during the period. The annual percentage yield earned (using the formula above) is 6.58%:

$$\text{APY Earned} = 100[(1 + 5.25/1{,}000)^{(365/30)} - 1]$$

APY Earned = 6.58%

(2) Assume a credit union calculates dividends on the average daily balance for the calendar month and provides periodic statements that cover the period from the 16th of one month to the 15th of the next month. The account has a balance of $2,000 September 1 through September 15 and a balance of $1,000 for the remaining 15 days of September. The average daily balance for the month of September is $1,500, which results in $6.50 in dividends earned for the month. The annual percentage yield earned for the month of September would be shown on the periodic statement covering September 16 through October 15. The annual percentage yield earned (using the formula above) is 5.40%:

$$\text{APY Earned} = 100[(1 + 6.50/1{,}500)^{(365/30)} - 1]$$

APY Earned = 5.40%

(3) Assume a credit union calculates dividends on the average daily balance for a quarter (for example, the calendar months of September through November), and provides monthly periodic statements covering calendar months. The account has a balance of $1,000 throughout the 30 days of September, a balance of $2,000 throughout the 31 days of October, and a balance of $3,000 throughout the 30 days of November. The average daily balance for the quarter is $2,000, which results in $21 in dividends earned for the quarter. The annual percentage yield earned would be shown on the periodic statement for November. The annual

percentage yield earned (using the formula above) is 4.28%:

$$\text{APY Earned} = 100\ [(1 + 21/2{,}000)^{(365/91)} - 1]$$

APY Earned = 4.28%

B. Special formula for use where periodic statement is sent more often than the period for which dividends are compounded.

Credit unions that use the daily balance method to accrue dividends and that issue periodic statements more often than the period for which dividends are compounded shall use the following special formula:

$$\text{APY Earned} = 100\ [\ !\ 1 + \frac{(\text{Dividends earned/Balance})}{\text{Days in period (Compounding)}}\ "\ (365/\text{Compounding})\ \cdot 1]$$

The following definition applies for use in this formula (all other terms are defined under Part II):

"Compounding" is the number of days in each compounding period.

Assume a credit union calculates dividends for the statement period using the daily balance method, pays a 5.00% dividend rate, compounded annually, and provides periodic statements for each monthly cycle. The account has a daily balance of $1000.00 for a 30-day statement period. The dividend earned of $4.11 for the period, and the annual percentage yield earned (using the special formula above) is 5.00%:

$$\text{APY Earned} = 100\ .\ !\ 1\P\ \frac{(\$4.11/1{,}000)}{30}(365)\ "\ ^{(365/365)}\ \cdot 1\ \%$$

Appendix B to Part 707—Model Clauses and Sample Forms

General Note: Appendix B contains model clauses and sample forms intended for optional use by credit unions to aid in compliance with the disclosure requirements of §§ 707.4 (account disclosures), 707.5 (subsequent disclosures), 707.6 (statement disclosures), and 707.8 (advertisements). Section 269(b) of TISA provides that credit unions that use these clauses and forms will be in compliance with TISA's disclosure provisions.

As discussed in the supplementary information to § 707.3(a), this final rule provides for flexibility in designing the format of the disclosures. Credit unions can choose to prepare a single document or brochure that incorporates disclosures for all accounts offered, or to prepare different documents for each type of account. Credit unions may also use inserts to a document, or fill in blanks to show current rates, fees and other terms.

In the model clauses, words in parentheses indicate the type of disclosure a credit union should insert in the space provided (for example, a credit union might insert "July 23, 1995" in the blank for a "(date)" disclosure). Brackets and "/" indicate that a credit union must choose the alternative that best describes its practice (for example, "[daily balance/ average daily balance]"). It should be noted that only in sections B–6 through B–10 of this appendix have specific examples of disclosures been given, with dates and figures. Sections B–1 through B–5, and section B–11 provide only unspecific model clauses or blank forms. The Board felt, as did the FRB in the Appendix A to Regulation DD, that a mix of blank clauses and forms and application of the model clauses to real specific situations would benefit those who must comply with TISA.

Any references to NCUA Rules and Regulations, the *NCUA Standard FCU Bylaws,* or the *NCUA Accounting Manual for FCUs*, are provided for guidance and as a point of reference for credit unions. Citations to these sources does not indicate that their application is required for those credit unions who need not follow them.

B–1 MODEL CLAUSES FOR ACCOUNT DISCLOSURES (§ 707.4(b))

(a) Rate Information (Sec.707.4(b)(1))

(i) *Fixed-Rate Accounts (§ 707.4(b)(1)(i)(A–B))*

1. Interest-bearing Accounts

The interest rate on your deposit account is _____% with an annual percentage yield (APY) of _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days].

Note: This provision reflects an accurate statement for an interest-bearing account authorized by state law for state-chartered credit unions. While the definition of the term "interest" permits its substitution for the term "dividends," separate disclosures should be made for interest-bearing accounts. Since account opening disclosures may be provided to potential members requesting account information before opening an account, and members opening new accounts, information is provided indicating that the rate may not be current, but that the potential member or member may call the credit union to obtain up-to-date information. When opening a new account, of course, a credit union could provide the contractual rate alone, and delete the sentences in brackets. Given the definition of fixed-rate account in § 707.2(n), credit unions offering fixed-rate accounts must contract to hold rates steady for at least a 30-day period. Thus, if the 30-day option of the last sentence is not chosen, the period chosen must be longer than 30 days.

2. Dividend-bearing Term Share Accounts

The dividend rate on your term share account is _____% with an annual percentage yield (APY) of _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days].

Note: This provision reflects an accurate statement for a fixed-rate, dividend-bearing

term share account. Interest-bearing term share accounts would use the disclosure in § 1, above. Since account opening disclosures may be provided to potential members requesting account information before opening an account, and members opening new accounts, information is provided indicating that the rate may not be current, but that the potential member or member may call the credit union to obtain up-to-date information. When opening a new account, of course, a credit union could provide the contractual rate alone, and delete the sentences in brackets. Given the definition of fixed-rate account in § 707.2(n), credit unions offering fixed-rate accounts must contract to hold rates steady for at least a 30-day period. Thus, if the 30-day option of the last sentence is not chosen, the period chosen must be longer than 30 days.

3. Other Dividend-bearing Accounts

[As of [the last dividend declaration date/(date)], the dividend rate was _____% with an annual percentage yield (APY) of _____% on your account./or The prospective dividend rate on your account is _____% with a prospective APY of _____% for the current dividend period.] You will be paid this rate for [(time period)/at least 30 calendar days].

or

[As of [the last dividend declaration date/(date)], the dividend rate was _____% with an annual percentage yield (APY) of _____% on your account./or The prospective dividend rate on your account is _____% with an annual percentage yield (APY) of _____% for this dividend period.] This rate will not change unless the credit union notifies you at least 30 calendar days prior to any change.

Note: Credit unions may disclose the dividend rate and annual percentage yield on accounts as of the last dividend declaration date. This necessitates inclusion of a disclosure of the actual calendar date of the last dividend declaration date. Additionally or alternatively (if the last dividend rate could be inaccurate), credit unions may disclose a prospective dividend rate and a prospective annual percentage yield. Such prospective rates and yields must be estimated in good faith, and must be declared at the proper time if it is at all possible to do so. As for the last sentence in these disclosures, this provision reflects a credit union policy to set prospective dividend rates for the next month (or at least 30 days), quarter or other period. Many credit unions, at their mid-monthly board meeting, set prospective dividend rates for the next month beginning on the 1st day of the month and continuing to the last day of the month. These rates must be formalized or ratified at the end of a dividend period. Given the timing of the board meetings, the time to prepare and mail notices and the 30 day period, it will often take credit unions 45 to 60 days to effectively change rates. For these reasons, the Board strongly suggests that credit unions do not offer fixed-rate, dividend-bearing accounts.

(ii) Variable-Rate Accounts (§ 707.4(b)(1)(ii))

1. Interest-bearing Accounts

The interest rate on your deposit account is _____%, with an annual percentage yield (APY) of _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] The interest rate and annual percentage yield may change every (time period) based on [(name of index)/the determination of the credit union board of directors]. The interest rate for your account will [never change by more than _____% each (time period)/never be less/more than _____%/never exceed _____% above or fall more than _____% below the initial interest rate].

Note: This disclosure combines the requirements of § 707.4(b)(1)(i) with § 707.4(b)(1)(ii) for interest-bearing accounts. The variable nature of a deposit account usually is based on an external index or is set at the discretion of the board. If another means of rate setting is used, that, instead of the proposed language, must be disclosed. Since account opening disclosures may be provided to potential members requesting account information before opening an account, and members opening new accounts, information is provided indicating that the rate may not be current, but that the potential member or member may call the credit union to obtain up-to-date information. When opening a new account, of course, a credit union could provide the contractual rate alone, and delete the sentences in brackets. Rarely would there be limitations on rate changes, but language is provided for this situation in the last sentence. Of

course, it is only to be used if it applies to an account.

2. Dividend-bearing Term Share Accounts

The dividend rate on your term share account is _____%, with an annual percentage yield (APY) of _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] The dividend rate and annual percentage yield may change every (time period) based on [(name of index)/the determination of the credit union board of directors]. The dividend rate for your account will [never change by more than _____% each (time period)/never be less/more than _____%/never exceed _____% above or fall more than _____% below the initial dividend rate].

Note: This disclosure combines the requirements of § 707.4(b)(1)(i) with § 707.4(b)(1)(ii) for dividend-bearing, variable-rate term share accounts. The variable nature of a deposit account usually is based on an external index or is set at the discretion of the board. If another means of rate setting is used, that, instead of the model language, must be disclosed. Since account opening disclosures may be provided to potential members requesting account information before opening an account, and members opening new accounts, information is provided indicating that the rate may not be current, but that the potential member or member may call the credit union to obtain up-to-date information. When opening a new account, of course, a credit union could provide the contractual rate alone, and delete the sentences in brackets. Rarely would there be limitations on rate changes, but language is provided for this situation in the last sentence. Of course, it is only to be used if it applies to an account.

3. Other Dividend-bearing Accounts

[As of [the last dividend declaration date/(date)], the dividend rate was _____% with an annual percentage yield (APY) of _____% on your account./or The prospective dividend rate on your account is _____% with an anticipated annual percentage yield (APY) of _____% for the current dividend period.] The dividend rate and annual percentage yield may change every (dividend period) as determined by the credit union board of directors.

Note: This language combines the requirements of § 707.4(b)(1)(i) with § 707.4(b)(1)(ii). Credit unions may disclose the dividend rate and annual percentage yield on accounts as of the last dividend declaration date. This necessitates inclusion of a disclosure of the actual calendar date of the last dividend declaration date or use of the phrase "last dividend declaration date". Additionally or alternatively, credit unions may disclose a prospective dividend rate and a prospective annual percentage yield. Such prospective rates and yields must be estimated in good faith, and must be declared at the proper time if it is at all possible to do so. As for the last sentence in these disclosures, this provision reflects the variable nature of the account. Generally, there is only one variable-rate feature for share accounts: the frequency of dividend period rate changes (e.g., daily, weekly, monthly, quarterly, semi-annually, annually). Normally, there are no contractual limitations on share account earnings (unless imposed by a regulator), nor are earnings based on any internal or external index. If contractual limitations or an index are involved, however, those factors would need to be disclosed (unless a regulator orders otherwise).

(iii) Stepped-Rate Accounts (§ 707.4(b)(1)(i))

1. Interest-bearing Accounts

The initial interest rate on your deposit account is _____%. You will be paid that rate [for (time period)/until (date)]. After that time, the interest rate for your deposit account will be _____% and you will be paid that rate [for (time period)/until (date)]. The annual percentage yield (APY) for your account is _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days].

2. Dividend-bearing Term Share Accounts

The initial dividend rate on your term share account is _____%. You will be paid that rate [for (time period)/until (date)]. After that time, the dividend rate for your term share account will be _____% and you

will be paid that rate [for (time period)/until (date)]. The annual percentage yield (APY) for your account is _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days].

3. Other Dividend-bearing Accounts

[As of [the last dividend declaration date/(date)], the initial dividend rate on your account was _____%./or The prospective dividend rate on your account is _____%.] You will be paid that rate [for (time period)/until (date)]. After that time, the prospective dividend rate for your share account will be _____% and you will be paid such rate [for (time period)/until (date)]. The annual percentage yield (APY) for your account is _____%. You will be paid this rate for [(time period)/at least 30 calendar days].

Note: Stepped-rate accounts are accounts with two or more rates that take effect in succeeding periods. The applicable rates and time periods are known when the account is opened. By nature these are fixed-rate accounts and are usually associated with term share (certificate) accounts. Accordingly, a contract provision (for share accounts) to change rates should be included.

(iv) Tiered-Rate Accounts (§ 707.4(b)(1)(i))

1. Interest-bearing Accounts

Tiering Method A

1* If your [daily balance/average daily balance] is $ _____ or more, the interest rate paid on the entire balance in your account will be _____%, with an annual percentage yield (APY) of _____%.

2* If your [daily balance/average daily balance] is more than $ _____, but less than $ _____, the interest rate paid on the entire balance in your account will be _____%, with an APY of _____%.

3* If your [daily balance/average daily balance] is $ _____ or less, the interest rate paid on the entire balance will be _____% with an APY of _____%.

[For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.]

[*Fixed-rate*—You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days]./*Variable-rate*—The interest rate and APY may change every (time period) based on [(name of index)/the determination of the credit union board of directors.]

Note: Tiering Method A pays the stated dividend rate that corresponds to the applicable account balance tier on the full balance in the account. This example contemplates a two-tier system. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. For tiered-rate accounts, a disclosure may be added about the currency of the rate, as is provided in the first set of brackets. A disclosure regarding the fixed-rate or variable-rate nature of the account must be added, as is provided in the last set of brackets.

Tiering Method B

1* A dividend rate of _____% will be paid only on the portion of your [daily balance/average daily balance] that is greater than $_____. The annual percentage yield (APY) for this tier will range from _____% to _____%, depending on the balance in the account.

2* A dividend rate of _____% will be paid only on the portion of your [daily balance/average daily balance] that is greater than $_____, but less than $_____. The annual percentage yield (APY) for this tier will range from _____% to _____%, depending on the balance in the account.

3* If your [daily balance/average daily balance] is $_____ or less, the dividend rate paid on the entire balance will be _____%, with an annual percentage yield (APY) of _____%.

[For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.]

[*Fixed-rate*—You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days]./*Variable-rate*—The interest

rate and APY may change every (time period) based on [(name of index)/the determination of the credit union board of directors.]

Note: Tiering Method B pays different stated dividend rates corresponding to applicable deposit tiers, on the applicable balance in each tier of the account. For example, a credit union might pay 3% dividend on account funds of $500 or below, and pay 4% dividend on the portion of the same account that exceeds $500. The example contemplates an account with two tiers, but additional tiers are possible. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. For tiered-rate accounts, a disclosure may be added about the currentness of the rate, as is provided in the first set of brackets.

Tiered-rate accounts can be either fixed-rate or variable-rate accounts. The last sentence offers an option of either fixed-rate or variable-rate disclosure. Thus, the disclosures outlined above will be made in addition to either: (i) disclosure of the period the fixed-rates are in effect or (ii) the variable-rate disclosures. Tiered-rate accounts are also subject to the requirement for disclosure of the balance computation method, *see* paragraph (e) to this appendix.

3. Other Dividend-bearing Accounts

Tiering Method A

1* [As of [the last dividend declaration date/(date)], if your [daily balance/average daily balance] was $_____ or more, the dividend rate paid on the entire balance in your account was _____%, with an annual percentage yield (APY) of _____%./or If your [daily balance/average daily balance] is $_____ or more, a prospective dividend rate of _____% will be paid on the entire balance in your account with a prospective annual percentage yield (APY) of _____% for this dividend period.]

2* [As of [the last dividend declaration date/(date)], if your [daily balance/average daily balance] was more than $_____, but was less than $_____, the dividend rate paid on the entire balance in your account was _____%, with an annual percentage yield (APY) of _____%./or If your [daily balance/average daily balance] is more than $_____, but is less than $_____, a prospective dividend rate of _____% will be paid on the entire balance in your account with a prospective annual percentage yield (APY) of _____% for this dividend period.]

3* [As of the last dividend declaration date/(date)], if your [daily balance/average daily balance] was $_____ or less, the dividend rate paid on the entire balance in your account will be _____% with an annual percentage yield (APY) of _____%./or If your [daily balance/average daily balance] is $_____ or less, the prospective dividend rate of_____% will be paid on the entire balance in your account with an annual percentage yield (APY) of _____% for this dividend period.]

[*Fixed-rate*—You will be paid this rate for [(time period)/at least 30 calendar days]./ *Variable-rate*—The dividend rate and APY may change every (dividend period) as determined by the credit union board of directors.]

Note: Tiering Method A pays the stated dividend rate that corresponds to the applicable deposit tier on the full balance in the account. This example contemplates a two-tier system. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. For tiered-rate accounts, a disclosure may be added about the prospective rate. Note that the prospective rate disclosure options match the required tiered-rate disclosures based on the previous dividend declaration date. A disclosure regarding the fixed-rate or variable-rate nature of the account must be added, as is provided in the last set of brackets.

Tiering Method B

1* [As of [the last dividend declaration date/(date)], a dividend rate of _____% was paid only on the portion of your [daily balance/average daily balance] that was greater than $_____. The annual percentage yield (APY) for this tier ranged from _____% to _____%, depending on the balance in the account./or A prospective dividend rate of _____% will be paid only on the portion of your [daily balance/average daily balance] that is greater than $_____ with a prospective annual percentage yield (APY) ranging from _____% to _____%, depending on the balance in the account, for this dividend period.]

2* [As of [the last dividend declaration date/(date)], a dividend rate of _____% was paid only on the portion of your [daily bal-

ance/average daily balance] that was greater than $_____ but less than $_____. The annual percentage yield (APY) for this tier ranged from _____% to _____%, depending on the balance in the account./or A prospective dividend rate of _____% will be paid only on the portion of your [daily balance/average daily balance] that is greater than $_____, but less than $_____] with a prospective annual percentage yield (APY) ranging from _____% to _____%, depending on the balance in the account, for this dividend period.]

3* [As of [the last dividend declaration date/(date)], if your [daily balance/average daily balance] was $_____ or less, the dividend rate paid on the entire balance was _____%, with an annual percentage yield (APY) of _____%./or If your [daily balance/average daily balance] was $_____ or less, the prospective dividend rate paid on the entire balance in your account will be _____% with a prospective annual percentage yield (APY) of _____% for this dividend period.]

Note: Tiering Method B pays different stated dividend rates corresponding to applicable account tiers, on the applicable balance in each tier of the account. For example, a credit union might pay a 3% dividend on account funds of $500 or below, and pay a 4% dividend on the portion of the same account that exceeds $500. The example contemplates an account with two tiers, but additional tiers are possible. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. Note that the prospective rate disclosure options match the required tiered-rate disclosures based on the previous dividend declaration date.

Tiered-rate accounts can be either fixed-rate or variable-rate accounts. The last sentence offers an option of either fixed-rate or variable-rate disclosures. Thus, the disclosures outlined above must be made in addition to either: (i) disclosure of the period the fixed-rates are in effect or (ii) the variable-rate disclosures. Tiered-rate accounts are also subject to the requirement for disclosure of the balance computation method, *see* paragraph (e) to this appendix.

(b) Nature of Dividends (§ 707.4(b)(8))

Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

Note: The Board of Directors declares dividends based on current income and available earnings of the credit union after providing for the required reserves at the end of the month. The dividend rate and annual percentage yield shown may reflect either the last dividend declaration date on the account or the earnings the credit union anticipates having available for distribution. This disclosure only applies to share and share draft (as opposed to deposit) accounts and should be grouped with the Rate Information to make the disclosures more meaningful. This disclosure also does not apply to term share accounts for reasons discussed in the supplementary information regarding §§ 707.3(e) and 707.4(b)(8).

(c) Compounding and Crediting (§ 707.4(b)(2))

[Dividends/Interest] will be compounded (frequency) and will be credited (frequency).

and, if applicable:

If you close your [share/deposit] account before [dividends/interest] [are/is] paid, you will not receive the accrued [dividends/interest].

and, if applicable (for dividend-bearing accounts):

For this account type, the dividend period is (frequency), for example, the beginning date of the first dividend period of the calendar year is (date) and the ending date of such dividend period is (date). All other dividend periods follow this same pattern of dates. The dividend declaration date follows the ending date of a dividend period, and for the example is (date).

Note: Where the word "(frequency)" appears, time periods must be inserted to coincide with those specified in board resolutions of each credit union's board of directors. A disclosure of dividend period was added to § 707.4(b)(2)(i) in the final rule to assist members in knowing when dividend rate and APY disclosures would be given by a credit union using the optional statement rule of § 707.6(a). The dividend declaration date is important for purposes of § 707.4(a)(2)(ii), request disclosures, § 707.4(b)(2), account opening disclosures, and § 707.8(c)(2), advertising disclosures. The Board believes that this is critical information for divi-

dend-bearing accounts, but that provision by an example (whether of the first dividend period of the year, or of any randomly chosen dividend period) is favorable to providing a list of such dates for the entire year or for a period of years (although these methods would also be permissible). As noted in the supplementary information to § 707.2(j), dividend declaration date, the dividend period and actual dividend distribution date may vary. Thus, it is possible for crediting periods and dividend periods not to coincide, though the Board believes that credit unions should make every effort to attempt to coordinate the two periods.

(d) Minimum Balance Requirements (§ 707.4 (b)(3)(i))

(i) *To open the account*

The minimum balance required to open this account is $_____.

or, for first share account at a credit union

The minimum required to open this account is the purchase of a (par value of a share) share in the credit union.

(ii) *To avoid imposition of fees*

You must maintain a minimum daily balance of $_____ in your account to avoid a service fee. If, during any (time period), your account balance falls below the required minimum daily balance, your account will be subject to a service fee of $_____ for that (time period).

or

You must maintain a minimum average daily balance of $_____ in your account to avoid a service fee. If, during any (time period), your average daily balance is below the required minimum, your account will be subject to a service fee of $_____ for that (time period).

(iii) *To obtain the annual percentage yield disclosed*

You must maintain a minimum daily balance of $_____ in your account each day to obtain the disclosed annual percentage yield.

or

You must maintain a minimum average daily balance of $_____ in your account to obtain the disclosed annual percentage yield.

(iv) *Absence of minimum balance requirements*

No minimum balance requirements apply to this account.

(v) *Par value*

The par value of a share in this credit union is $_____.

Note: Where the words "(time period)" appear, time periods should be inserted to coincide with those specified in board resolutions of each credit union's board of directors. As the supplementary information to § 707.4(b)(3)(i) explains, the par value of a share to establish membership is a critical disclosure to be made to potential members of credit unions. The par value disclosure is required by § 707.4(b)(3)(i) as being analogous to a minimum balance account opening requirement.

(e) Balance Computation Method (§ 707.4(b)(3)(ii))

(i) *Daily Balance Method*

[Dividends/Interest] [are/is] calculated by the daily balance method which applies a daily periodic rate to the balance in the account each day.

(ii) *Average Daily Balance Method*

[Dividends/Interest] [are/is] calculated by the average daily balance method which applies a periodic rate to the average daily balance in the account for the period. The average daily balance is calculated by adding the balance in the account for each day of the period and dividing that figure by the number of days in the period.

Note: Any explanation of balance computation method must contain enough information for members to grasp the means by which dividends or interest will be calculated on their accounts. Using a shorthand form, such as "day in/day out" for the daily balance method or "average balance" for the average daily balance method, without more information, is insufficient. In addition, any disclosure based on the equivalency of the two allowable methods, such as stating that the average daily balance method was the same as the daily balance method, is impermissible and misleading.

(f) Accrual of Dividends/Interest on Noncash Deposits (§ 704.4(b)(3)(iii))

[Dividends/Interest] will begin to accrue on the business day you [place/deposit] noncash items (e.g. checks) to your account.

or

[Dividends/Interest] will begin to accrue no later than the business day we receive provisional credit for the [placement/deposit] of noncash items (e.g. checks) to your account.

Note: Accrual information is not included in the explanation of balance computation method required by § 707.4(b)(4)(ii). In addition, the disclosures required by TISA do not affect the substantive requirements of the EFAA and Regulation CC. The EFAA and Regulation CC control, and any modifications to them should occasion credit unions to revisit this disclosure with a view to revising it to reflect current law.

(g) Fees and Charges (§ 707.4(b)(4))

The following fees and charges may be assessed against your account:
(service/explanation) $_____
(service/explanation) $_____

Note: Fees and charges may be disclosed in an account disclosure, or separately in a Rate and Fee Schedule (see section B–11 of this appendix). In either event, the disclosure should also specify when the fee will be assessed by using phrases such as "per item," "per month," or "per inquiry."

(h) Transaction Limitations (§ 707.4(b)(5))

The minimum amount you may [withdraw/write a draft for] is $_____.

During any statement period, you may not make more than six withdrawals or transfers to another credit union account of yours or to a third party by means of a preauthorized or automatic transfer or telephonic order or instruction. No more than three of the six transfers may be made by check, draft, debit card, if applicable, or similar order to a third party. If you exceed the transfer limitations set forth above in any statement period, your account will be subject to [closure by the credit union/a fee of $_____].

Note: This paragraph satisfies the requirements of § 707.4(b)(6) with respect to Regulation D limitations on share accounts and money market accounts. These are some of the more common limitations applicable.

The credit union reserves the right to require a member intending to make a withdrawal from any account (except a share draft account) to give written notice of such intent not less than seven days and up to 60 days before such withdrawal.

Note: This disclosure is limted to federal credit unions with Bylaws containing this limitation. See Standard Federal Credit Union Bylaws, Art. III, § 5(a). Similar disclosures are required of any state-chartered credit unions having similar limitations in their bylaws, or under state law. This limitation does not directly relate to the "number" or "amount" of transactions, and accordingly, may not be necessary under § 707.4(b)(5), but would, if applicable, be required by § 707.3(b).

(i) Disclosures related to term share accounts (§ 707.4(b)(6))

(i) *Time requirements*

Your account will mature on (date).

or

Your account will mature after (time period).

(ii) *Early withdrawal penalties*

We [will/may] impose a penalty if you withdraw [any/all] of the [funds/principal] in your account before the maturity date. The penalty will equal [_____ days'/weeks'/months'] [dividends/interest] on your account.

or

We [will/may] impose a penalty of $_____ if you withdraw [any/all] of the [funds/principal] before the maturity date.

If you withdraw some of your funds before maturity, the [dividend/interest] rate for the remaining funds in your account will be _____%, with an annual percentage yield of _____%.

Note: In most cases, the dividend rate and annual percentage yield on the funds remaining in the account after early withdrawal are the same as before the withdrawal. Accordingly, the disclosure of dividend rate and annual percentage yield after withdrawal is required only if the dividend rate and APY will change.

(iii) *Withdrawal of dividends/interest prior to maturity*

The annual percentage yield is based on an assumption that [dividends/interest] will remain in the account until maturity. A withdrawal will reduce earnings.

Note: This disclosure may be used if the credit union compounds dividends/interest and allows withdrawal of accrued dividends/interest before maturity. This disclosure alerts members that the annual percentage yield is based on an

assumption that the dividends/interest remain on deposit until maturity.

(iv) *Renewal policies*

1. *Automatically renewable term share accounts*

Your term share account will automatically renew at maturity. You will have a grace period of _____ [calendar/business] days after the maturity date to withdraw the funds in the account without being charged an early withdrawal penalty.

or

Your term share account will automatically renew at maturity. There is no grace period following the maturity of this account.

2. *Non-automatically renewable term share accounts*

This account will not renew automatically at maturity. If you do not renew the account, your account will [continue to earn/ no longer earn] [dividends/interest] after the maturity date.

Note: These disclosures should agree with the necessary prematurity notices for term share accounts in B–3 of this appendix.

(v) *Required dividend distribution.*

This account requires the distribution of dividends and does not allow dividends to remain in the account.

(j) Bonuses (§ 704.4(b)(7))

You will [be paid/receive] [$_____/ (description of item)] as a bonus [when you open the account/on (date)].

You must maintain a minimum [daily balance/ average daily balance] of $_____ to obtain the bonus.

To earn the bonus, [$_____/your entire principal] must remain on deposit [for (time period)/until (date)].

Note: These disclosures follow the requirements of § 707.4(b)(7) and should be used as applicable. Further information may also be added, especially if it clarifies the conditions and timing of receiving the bonus, or better informs the member about the bonus.

B–2 MODEL CLAUSES FOR CHANGES IN TERMS (§ 707.5(a))

On (date), the (type of fee) will increase to $_____. On (date), the [dividend/interest] rate on your account will decrease to _____%, with an annual percentage yield (APY) of _____%.

On (date), the [minimum daily balance/ average daily balance] required to avoid imposition of a fee will increase to $_____.

Note: These examples apply to the more common changes necessitating a changes in terms notice. However, any change, amendment or modification reducing the APY or adversely affecting the members holding such accounts must be disclosed. For such changes not contemplated by the model clauses, the Board recommends the use of as simple language as possible to convey the change, along with cross-referencing to the particular sections or paragraph numbers of the account opening disclosures, when to do so will assist members in reviewing and understanding the change.

B–3 MODEL CLAUSES FOR PRE-MATURITY NOTICES FOR TERM SHARE ACCOUNTS (§ 707.5(b–d))

(a) *Maturity date*

Your term share account will mature on _____.

(b) *Nonrenewal*

Unless your term share account is renewed, it will not accrue further [dividends/ interest] after the maturity date.

(c) *Rate information*

The [dividend/interest] rate and annual percentage yield that will apply to your term share account if it is renewed have not yet been determined. That information will be available on _____. After that date, you may call the credit union during regular business hours at (telephone number) to find out the [dividend/interest] rate and annual percentage yield (APY) that will apply to your term share account if it is renewed.

Note: Pre-maturity notices should follow the requirements of § 707.5(b–d) as closely as possible. Care should be taken to explain any grace periods used. See discussion of use of alternative timing in supplementary information to § 707.2(o) and § 707.5(b–d).

B–4 SAMPLE FORM (SIGNATURE CARD/ APPLICATION FOR MEMBERSHIP)

SIGNATURE CARD/APPLICATION FOR MEMBERSHIP

ACCOUNT NUMBER _____

_____ _____ _____
(last name) (first name) (middle name)

_____ _____
(street address) (apartment no.)

_____ _____ _____
(city) (state) (zip code)

_____ _____
(home telephone no.) (business telephone no.)

_____ _____
(Social Security # or TIN) (date of birth)

_____ _____
(mother's maiden name) (employer, occupation)

I hereby make application for membership in and agree to conform to the Bylaws, as amended, of _____ Credit Union (the "Credit Union"). I certify that: I am within the field of membership of this Credit Union; the information provided on this application is true and correct; and my signature on this card applies to all accounts under my name at this Credit Union. I also agree to be bound to the terms and conditions of any account that I have in the Credit Union now or in the future.

_____
(signature of applicant)

This application approved _____ (date) by the (Check one)
( ) Board ( ) Exec. Committee ( ) Membership Officer

Signed: _____
(Secretary; Exec. Cmte. Member, or Membership Officer)

Note: This form is modeled on NCUA Form FCU 150, Application for Membership, as discussed in the Accounting Manual for FCUs, §§ 5030.1, 5150.3. It is noted that other information can also be requested on the signature card, as long as it is in accordance with federal and state laws. For example, information identifying the member, such as a state driver's license number, could be added. The types of accounts that the signature applies to could be specified. Furthermore, the Board notes that this card contains much identification information that may not be necessary for all credit unions; common sense should guide credit union boards of directors in designing their applications for membership/signature cards. However, the Board believes that the information solicited on this form is reasonable and prudent for many credit unions. Payable on death designations, joint account language required under state law, life savings beneficiary designations, and other like variations and designations may be added to the card if so desired. The proposed signature card/ application for membership form contained taxpayer certification language. One commenter noted that the IRS may always change its requirements in this area, which are beyond the authority of the Board. Therefore, the Board has deleted reference to the IRS taxpayer certification required by 26 USC 3406, but notes that such certification must be made in accordance with applicable law and IRS rules. The information may be included on the front and back of a standard size signature card, or on the front of a large size signature card. However, no account terms may be included on a signature card unless a copy of the signature card is provided to the member at the time of account opening. The Board recommends that credit unions refrain from this practice, and instead use standard account disclosures. One reason for this is that if laws, regulations or credit union policies change, discrepancies may result between them and the earlier signature card terms. Given the longevity of credit union membership, signature cards may well be in use for up to or over a century. In addition, as signature cards are relatively small, they probably will not contain enough space to make all desired and required disclosures. Fragmentation of terms, some on signature cards, some on separate disclosures, could easily lead to member confusion. As terms are usually construed against the drafter, credit unions should be very careful in their use of account terms and conditions varying from those provided as model clauses and sample forms in this appendix.

B–5 SAMPLE FORM (TERM SHARE [CERTIFICATE] ACCOUNT)

TERM SHARE (CERTIFICATE) ACCOUNT

_____ _____
Date Issued Account Number

_____ _____
Certificate Number Social Security Number

This is to certify that (name(s)) _____ [is/are] the owner(s) of a term share certificate account in the _____ Credit Union (the "Credit Union") in the amount of _____ Dollars ($_____). This term share certificate account may be redeemed on (maturity date) _____ only upon presentation of the certificate to the Credit Union. The divi-

dend rate of this certificate account is _____% with an annual percentage yield of _____%. The annual percentage yield and dividend rate assume that dividends are to be [check one] ( ) added to principal/ ( ) paid to regular share account number _____/( ) mailed to owner(s). This account is subject to all terms and conditions stated in the Term Share Certificate Account Disclosures, as they may be amended from time to time, and incorporates the same by reference into this agreement.

_____
Authorized signature

_____
Authorized signature

Note: This form is modeled on NCUA Form FCU 107SCP, Credit Union Share Certificate, as discussed in the Accounting Manual for FCUs, §§ 5030.1, 5150.6. It is simplified to reflect the term share (certificate) account agreement, the parties involved, the maturity term and the annual percentage yield and dividend rate. All other terms are incorporated by reference. This should allow the credit union maximum flexibility in fashioning certificate, and other term share account, products. If a credit union so desired, other terms and conditions could be incorporated into the term share certificate itself, as long as a copy is presented to the member at the account opening. Care should also be taken to ensure that the term share certificate format addresses any necessary state law concerns. As the FRB's Regulation D on reserve requirements permits all term share accounts to be represented by a transferable or nontransferable, or a negotiable or nonnegotiable, certificate, instrument, passbook, statement or otherwise, and still be considered a "time deposit", the Board has made no entry on this sample form regarding such terms, leaving the decision instead to each credit union's board of directors. 12 CFR 202.4(c)(2).

B–6 SAMPLE FORM (REGULAR SHARE ACCOUNT DISCLOSURES)

REGULAR SHARE ACCOUNT DISCLOSURES

1. *Rate information.* As of April 1, 1995, the dividend rate was 5.00% and the annual percentage yield (APY) was 5.13% on your regular share account. In addition, the credit union estimates a prospective dividend rate of 5.25% and a prospective APY of 5.39% on your share account for this dividend period. The divident rate and annual percentage yield may change every quarter as determined by the credit union board of directors.

2. *Compounding and crediting.* Dividends will be compounded daily and will be credited quarterly. For this account type, the dividend period is quarterly, for example, the beginning date of the first dividend period of the calendar year is January 1 and the ending date of such dividend period is March 31. All other dividend periods follow this same pattern of dates. The dividend declaration date follows the ending date of a dividend period, and for the example is April 1. If you close your regular share account before dividends are credited, you will not receive accrued dividends.

3. *Minimum balance requirements.* The minimum balance to open this account is the purchase of a $5 share in the Credit Union. You must maintain a minimum daily balance of $500 in your account to avoid a service fee. If, during any day during a quarter, your account balance falls below the required minimum daily balance, your account will be subject to a service fee of $5 for that quarter.

4. *Balance computation method.* Dividends are calculated by the daily balance method which applies a daily periodic rate to the principal in your account each day.

5. *Accrual of dividends.* Dividends will begin to accrue on the business day you deposit noncash items (e.g., checks) to your account.

6. *Fees and charges.* The following fees and charges may be assessed against your account.

a. Statement copies	$5.00 per statement
b. Account inquiries	$3.00 per inquiry
c. Dormant account fee	$10.00 per month
d. Wire transfers	$8.00 per transfer
e. Minimum balance service fee.	$5.00 per quarter
f. Share transfer	$1.00 per transfer
g. Excessive share	$1.00 per item withdrawals

7. *Transaction limitations.* During any statement period, you may not make more than six withdrawals or transfers to another credit union account of yours or to a third party by means of a preauthorized or automatic transfer or telephonic order or

instruction. No more than three of the six transfers may be made by check, draft, debit card, if applicable, or similar order to a third party. If you exceed the transfer limitations set forth above in any statement period, your account will be subject to closure by the credit union or to a fee of $1.00 per item.

8. *Nature of dividends.* Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

9. *Bylaw Requirements.* A member who fails to complete payment of one share within _____ of his admission to membership, or within _____ from the increase in the par value in shares, or a member who reduces his share balance below the par value of one share and does not increase the balance to at least the par value of one share within _____ of the reduction may be terminated from membership at the end of a dividend period. [All blanks should be filled with time chosen by credit union board of directors, but must be at least 6 months.] Shares may be transferred only from one member to another, by written instrument in such form as the Credit Union may prescribe. The Credit Union reserves the right, at any time, to require members to give, in writing, not more than 60 days notice of intention to withdraw the whole or any part of the amounts so paid in by them. No member may withdraw shareholdings that are pledged as required on security on loans without the written approval of the credit committee or a loan officer, except to the extent that such shares exceed the member's total primary and contingent liability to the Credit Union. No member may withdraw any shareholdings below the amount of his/her primary or contingent liability to the Credit Union if he/she is delinquent as a borrower, or if borrowers for whom he/she is comaker, endorser, or guarantor are delinquent, without the written approval of the credit committee or loan officer.

10. *Par value of shares; Dividend period.* The par value of a regular share in this Credit Union is $5. The dividend period of the Credit Union is quarterly.

11. *National Credit Union Share Insurance Fund.* Member accounts in this Credit Union are federally insured by the National Credit Union Share Insurance Fund.

12. *Other Terms and Conditions.* [In this item, which may be titled or subdivided in any manner by each credit union, NCUA suggests that the following issues be covered or handled: statutory lien or setoff; expenses (garnishments and bankruptcy orders and holds on account); joint ownership accounts; trust accounts; payable-on-death accounts; retirement accounts; Uniform Transfer to Minor Act accounts; sole proprietorship accounts; escrow and custodial accounts; corporation accounts; not-for-profit corporation accounts; voluntary association accounts; partnership accounts; public unit accounts; powers of attorney (guardianship orders); tax disclosures and certifications; Uniform Commercial Code variances; amendments; reliance on signature card; change of address; incorporations of other documents by reference, such as expedited funds availability policies, service charges schedules or electronic banking disclosures; ability to suspend services; and operational matters (stop payment orders—verbal and written, satisfactory identification, refusal of deposits not in proper form, wire transfers, stale check deposits, availability of periodic statements or passbook feature.)]

Note: This form is modeled on the share account disclosures in the Accounting Manual for FCUs, § 5150.7. The disclosures are for a variable-rate, daily balance method dividend calculation regular share account in an FCU with a $500 minimum balance to avoid service fees. For the example, the account was opened on May 1, 1995. Other terms are self-explanatory. The dividend rate paid and annual percentage yield disclosures will reflect the prospective dividend rate for a given dividend period. Item nos. 1–8 reflect standard TISA and part 707 disclosures discussed in sections B–1 through B–3 of this Appendix. Note that if the credit union limits the maximum amount of shares which may be held by one member under NCUA Standard FCU Bylaws, Art. III, § 2, that this should be stated in item no. 7, transaction limitations. Item no. 9 reflects various terms provided in Art. III, §§ 3–6 of the NCUA Standard FCU Bylaws. If this were a passbook account, then the requirements of Art. IV, Receipting for Money—Passbooks, in the NCUA

Standard FCU Bylaws would also be included in item no. 9. Item no. 10 reflects the par value amount of regular shares in a federal credit union, pursuant to section 117 of the FCU Act, 12 USC 117, and Art. XIV, § 3 of the NCUA Standard FCU Bylaws. It also states the dividend period of the credit union, which is set by the board of directors. Item no. 11 addresses the requirements of 12 CFR part 740. Nonfederally insured credit unions (NICUs) would be expected to disclose information required by section 151 of the Federal Deposit Insurance Corporation Improvement Act of 1991. 12 USC 1831t. By December 19, 1992, all NICUs were required to include conspicuously on all periodic statements of account, signature cards, passbooks, share certificates and other similar instruments of deposit and in all advertising a notice that the credit union is not federally insured. Additional disclosures will be required of NICUs by June 19, 1994. Item no. 12 is inserted to ensure that credit unions add other account terms and conditions not covered by the proposed regulation. These sorts of terms are contemplated by proposed § 707.3(b), requiring that the disclosures reflect the terms of the legal obligation between the member and the credit union. This list is not meant to be exhaustive, but to give a general idea of other topics often covered in share account contracts. Item no. 12 is not expressly required by either TISA or part 707, but any of these terms that are disclosed must be accurate and not misleading. Also the Board strongly recommends that such terms are included in account opening disclosures to inform the membership and to clearly set forth the legal relationship between the members and their credit union.

B–7 SAMPLE FORM (SHARE DRAFT ACCOUNT DISCLOSURES)

SHARE DRAFT ACCOUNT DISCLOSURES

1. *Rate information.* As of January 1, 1995, the dividend rate was 3.00% and the annual percentage yield (APY) was 3.04% on your share account. In addition, the prospective dividend rate on your account is 3.15% with a prospective annual percentage yield (APY) of 3.20% for the current dividend period. The dividend rate and APY may change every dividend period as determined by the credit union board of directors.

2. *Compounding and crediting.* Dividends will be compounded monthly and will be credited monthly. For this account type, the dividend period is monthly, for example, the beginning date of the first dividend period of the calendar year is January 1 and the ending date of such dividend period is January 31. All other dividend periods follow this same pattern of dates. The dividend declaration date follows the ending date of a dividend period, and for the example above is February 1. If you close your share draft account before dividends are credited, you will not receive accrued dividends.

3. *No minimum balance requirements apply to this account.*

4. *Balance computation method.* Dividends are calculated by the average daily balance method which applies a periodic rate to the average daily balance in the account for the period. The average daily balance is calculated by adding the balance in the account for each day of the period and dividing that figure by the number of days in the period.

5. *Accrual of dividends.* Dividends will begin to accrue no later than the business day we receive provisional credit for the placement of noncash items (e.g. checks) to your account.

6. *Fees and charges.* The following fees and charges may be assessed against your account.

a. Statement copies	$5.00 per statement
b. Account inquiries	$3.00 per inquiry
c. Dormant account fee	$10.00 per month
d. Wire transfers	$8.00 per transfer
e. Overdrafts/Returned Items.	$5.00 per draft
f. Share transfer	$1.00 per transfer
g. Excessive share withdrawal.	$1.00 per item
h. Certified checks	$5.00 per check
i. Stop Payment Order ..	$5.00 per order
j. Check Printing Fee	$12.00 per 200 checks (varies depending on style of check ordered)

7. *No transaction limitations apply to this account.*

8. *Nature of dividends.* Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

9. *Bylaw Requirements.* A member who fails to complete payment of one share within _____ of his admission to membership, or within _____ from the increase in the par value in shares, or a member who reduces his share balance below the par value of one share and does not increase the

balance to at least the par value of one share within _____ of the reduction may be terminated from membership at the end of a dividend period. [All blanks should be filled with time chosen by credit union board of directors, but must be at least 6 months.] Shares may be transferred only from one member to another, by written instrument in such form as the Credit Union may prescribe. The Credit Union reserves the right, at any time, to require members to give, in writing, not more than 60 days notice of intention to withdraw the whole or any part of the amounts so paid in by them. Shares paid in under an accumulated payroll deduction plan may not be withdrawn until credited to a member's account. No member may withdraw shareholdings that are pledged as required on security on loans without the written approval of the credit committee or a loan officer, except to the extent that such shares exceed the member's total primary and contingent liability to the Credit Union. No member may withdraw any shareholdings below the amount of his/her primary or contingent liability to the Credit Union if he/she is delinquent as a borrower, or if borrowers for whom he/she is comaker, endorser, or guarantor are delinquent, without the written approval of the credit committee or loan officer.

10. *Par value of shares; Dividend period.* The par value of a regular share in this Credit Union is $5. The dividend period of the Credit Union is monthly, beginning on the first of a month and ending on the last day of the month.

11. *National Credit Union Share Insurance Fund.* Member accounts in this Credit Union are federally insured by the National Credit Union Share Insurance Fund.

12. *Other Terms and Conditions.* [See section B–6, item 12, of this appendix].

Note: This form is modeled on the share account disclosures in the Accounting Manual for FCUs, §5150.7. The disclosures are for a variable-rate, average daily balance method dividend calculation share draft account in an FCU with no minimum balance requirement. For purposes of this example, the account was opened on January 15, 1995. The Credit Union has monthly dividend periods. Other terms are self-explanatory. The dividend rate paid and annual percentage yield disclosures will reflect the prospective dividend rate for a given dividend period. The disclosures are very similar to the ones in section B–6 of Appendix B, except for the rollback and par value disclosures, which have been removed from the final rule and appendices.

B–8 SAMPLE FORM (MONEY MARKET SHARE ACCOUNT DISCLOSURES)

MONEY MARKET SHARE ACCOUNT DISCLOSURES

1. *Rate information.* As of January 1, 1995, if your average daily balance was $500 or more, the dividend rate paid on the entire balance in your account was 4.75%, with an annual percentage yield (APY) of 4.85%. If your average daily balance is $500 or more, a prospective dividend rate of 4.95% will be paid on the entire balance in your account with a prospective APY of 5.00% for this dividend period on your account. The dividend rate and APY may change every dividend period as determined by the credit union board of directors.

2. *Compounding and crediting.* Dividends will be compounded monthly and will be credited quarterly. If you close your share money market account before dividends are credited, you will not receive accrued dividends.

3. *Minimum balance requirements.* The minimum balance required to open this account is $500. You must maintain a minimum daily balance of $500 in your account to avoid a service fee. If, during any (time period), your account falls below the required minimum daily balance, your account will be subject to a service fee of $5 for that (time period).

4. *Balance computation method.* Dividends are calculated by the average daily balance method which applies a periodic rate to the average daily balance in your account for the period. The average daily balance is calculated by adding the principal in the account for each day of the period and dividing that figure by the number of days in the period.

5. *Accrual of dividends.* Dividends will begin to accrue on the business day you deposit noncash items (e.g., checks) to your account.

6. *Fees and charges.* The following fees and charges may be assessed against your account.

a. Statement copies	$5.00 per statement
b. Account inquiries	$3.00 per inquiry
c. Dormant accountee	$10.00 per month
d. Wire transfers	$8.00 per transfer
e. Minimum balance service fee.	$5.00 per time period
f. Share transfer	$1.00 per transfer
g. Excessive share withdrawals.	$1.00 per item
h. Certified checks	$5.00 per check
i. Stop Payment Order ..	$5.00 per order
j. Check Printing Fee	$12.00 per 200 checks (varies depending on style of check ordered)

7. *Transaction limitations.* During any statement period, you may not make more than six withdrawals or transfers to another credit union account of yours or to a third party by means of a preauthorized or automatic transfer or telephonic order or instruction. No more than three of the six transfers may be made by check, draft, debit card, if applicable, or similar order to a third party. If you exceed the transfer limitations set forth above in any statement period, your account will be subject to closure by the credit union or to a fee of $1.00 per item.

8. *Nature of dividends.* Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

9. *Bylaw Requirements.* [This section should reflect any requirements concerning share accounts in the FISCU's bylaws or charter.]

10. *Par value of shares; Dividend period.* The par value of a regular share in this Credit Union is $50. The dividend period of the Credit Union is monthly, beginning on the first of a month and ending on the last day of the month.

11. *National Credit Union Share Insurance Fund.* Member accounts in this Credit Union are federally insured by the National Credit Union Share Insurance Fund.

12. *Other Terms and Conditions.* [See section B–6, item 12, of this appendix.]

Note: This form is modeled on the share account disclosures in the Accounting Manual for FCUs, § 5150.7 and on the share draft account disclosures in section B–7 of this appendix. The disclosures are for a variable-rate, tiered-rate (method A, option 1), average daily balance method dividend calculation, money market share account in a FISCU with a $500 minimum balance to open the account and to avoid service fees. For purposes of this example, the account was opened on January 29, 1995. Other terms are self-explanatory. The dividend rate paid and annual percentage yield disclosures will reflect the prospective dividend rate for a given dividend period. Note that the contents of Item 9, Bylaw requirements, must be tailored to the specific bylaws of a FISCU or NICU. Also note the high par value amount in Item 10.

B–9 SAMPLE FORM (TERM SHARE [CERTIFICATE] ACCOUNT DISCLOSURES)

TERM SHARE (CERTIFICATE) ACCOUNT DISCLOSURES

1. *Rate information.* [Repeat rates disclosed on face of term share certificate, see B–5, Sample Form (Term Share (Certificate) Account).]

2. *Compounding and crediting.* Dividends will be compounded monthly and will be credited annually. If you close your certificate account before dividends are credited, you will not receive accrued dividends.

3. *Minimum balance requirements.* The minimum balance required to open this account is $500.

4. *Balance computation method.* Dividends are calculated by the daily balance method, which applies a daily periodic rate to the principal in your account each day.

5. *Accrual of dividends.* Dividends will begin to accrue on the business day you deposit noncash items (e.g., checks) to your account.

6. *Fees and charges.* The following fees and charges may be assessed against your account.

a. Statement copies	$5.00 per statement
b. Account inquiries	$3.00 per inquiry
c. Share transfer	$1.00 per transfer

7. *Transaction limitations.* After the account is opened, you may not make deposits into the account until the maturity date stated on the certificate.

8. *Maturity date.* Your account will mature on January 1, 1996.

9. *Early withdrawal penalties.* We may impose a penalty if you withdraw any of the funds before the maturity date. The penalty will equal three months' dividends on your deposit.

10. *Renewal policies.* Your certificate account will automatically renew at matu-

rity. You will have a grace period of 10 business days after the maturity date to withdraw the funds in the account without being charged an early withdrawal penalty.
11. *Bonus.* You will receive a new (insert brand name) toaster-oven as a bonus when you open the account after December 31, 1994, and before June 30, 1995. You must maintain your entire principal on deposit until the maturity date of your certificate account to obtain the bonus.
12. **[RESERVED]**
13. *Bylaw Requirements.* [This section should reflect any requirements concerning share accounts in the FISCU's bylaws or charter.]
14. *Par value of shares; Dividend period.* The par value of a regular share in this Credit Union is $25. The dividend period of the Credit Union on this type of account is annual, beginning on the date the account is opened, and ending on the stated maturity date, unless renewed.
15. *National Credit Union Share Insurance Fund.* Member accounts in this Credit Union are federally insured by the National Credit Union Share Insurance Fund.
16. *Other Terms and Conditions.* [See section B–6, item 12, of this appendix.]

Note: Even though this disclosure is for an account at a FISCU, this form is modeled on the share account disclosures in the Accounting Manual for FCUs, § 5150.7 and upon the regular share account disclosures in section B–6 of this appendix. The disclosures are for a fixed-rate, daily balance method dividend calculation, automatically renewing term share certificate account in a FISCU with a $500 minimum balance to open the account and a ten day grace period. For the example, the account is opened on January 1, 1995 and matures on January 1, 1996. Other terms are self-explanatory. The dividend rate paid and annual percentage yield disclosures reflect the contracted, prospective dividend rate for a given dividend period. Note the special disclosures for term share certificate accounts, items nos. 8–10. Note also the bonus disclosure, item no. 11.

B–10 SAMPLE FORM (PERIODIC STATEMENT)

PERIODIC STATEMENT

_____ _____
Member Name Account Number

[Transaction account activity by date]

[Average daily balance of $1,500 for the month, daily compounding]

Your account earned $6.72, with an annual percentage yield earned of 5.40%, for the statement period from May 1 through and including May 31. In addition, your account earned $15 in extraordinary dividends for this period. Any fees assessed against your account are shown in the body of the periodic statement and are identified by the code at the bottom margin of this statement.

Service charge codes

SC-1 Stop Payment Order Fee
SC-2 Statement Copy Fee
SC-3 Draft Return Fee
SC-4 Transfer from Shares
SC-5 Microfilm Copy
SC-6 Share Draft Printing Fee
SC-7 Dormant Account Fee
SC-8 Wire Transfer Fee
SC-9 Excessive Share Withdrawal Fee
SC-10 _____

Other transactions

D=Dividends
EC=Error Correction
OR=Overdraft Returned
OL=Overdraft Loan
OS=Overdraft Share Transfer

Note: This form is modeled on the share draft statement of account, Form FCU 107G-SD, in the Accounting Manual for FCUs, § 5150.4. All information is self-explanatory. Codes of transactions are not required, but are a common credit union practice. The information regarding fees could also be included on the line of the periodic statement showing when the fees were debited from the account. Alternatively, a credit union could show all fees debited against the account for the statement period in a special area of the periodic statement. Clarity to the member of the required information—annual percentage yield earned; amount of dividends; fees imposed and length of period—is the important goal. An additional disclosure regarding the dollar value of any extraordinary dividends earned must be added to those statements showing the payment of such extraordinary dividends to the member.

B–11 SAMPLE FORM (RATE AND FEE SCHEDULE)

RATE AND FEE SCHEDULE

This Rate and Fee Schedule for all Accounts sets forth certain conditions, rates, fees and charges applicable to your regular share, share draft, and money market accounts at the _____ Federal Credit Union as of _____ [insert date of delivery to member]. This schedule is incorporated as part of your account agreement with the _____ Federal Credit Union.

REGULAR SHARE

Dividend Rate as of Last Dividend Declaration Date _____%

Annual Percentage Yield as of Last Dividend Declaration Date _____%

Prospective Dividend Rate _____%

Prospective Annual Percentage Yield _____%

Dividends Compounded [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Dividends Credited—At close of a dividend period

Dividend Period [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Minimum Opening Deposit $5.00 par value share

Minimum Monthly Balance [None, $ amount]

SHARE DRAFT

Dividend Rate as of Last Dividend Declaration Date _____%

Annual Percentage Yield as of Last Dividend Declaration Date _____%

Prospective Dividend Rate _____%

Prospective Annual Percentage Yield _____%

Dividends Compounded [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Dividends Credited—At close of a dividend period

Dividend Period [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Minimum Opening Deposit [None, $ amount]

Minimum Monthly Balance [None, $ amount]

MONEY MARKET

Dividend Rate as of Last Dividend Declaration Date _____%

Annual Percentage Yield as of Last Dividend Declaration Date _____%

Prospective Dividend Rate _____%

Prospective Annual Percentage Yield _____%

Dividends Compounded [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Dividends Credited— At close of a dividend period

Dividend Period [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Minimum Opening Deposit [None, $ amount]

Minimum Monthly Balance [None, $ amount]

The following fees may be assessed in connection with your accounts:

Fees Applicable to All Accounts:	
Returned item fee	$____.00 per item
Account reconciliation fee.	$____.00 per hour
Statement copies fee	$____.00 per statement
Certified draft fee	$____.00 per draft
Wire	$____.00 per transfer
Account inquiry fee	$____.00 per inquiry
Dormant account fee	$____.00 per month
Minimum balance service fee.	$____.00 per day
Share transfer fee	$____.00 per Transfer
Excessive share withdrawal transfer fee.	$____.00 per item
Share Draft Account Fees:	
Monthly service fee	$____.00 per month
Overdraft transfers fee	$____.00 per overdraft
Drafts returned insufficient funds fee.	$____.00 per draft
Stop payment order fee	$____.00 per order
Draft copy fee	$____.00 per copy
Check printing fee	$____.00 per 200 drafts
Money Market Share Account Fees:	
Monthly service fee	$____.00 per month
Check printing fee	$____.00 per 200 drafts

Note: This illustration is for use of an FCU. The information provided on a Rate and Fee Schedule can be presented in any format. To ensure that it is a part of the account agreement, if used, it should be incorporated by reference into the appropriate share account disclosures. The figures used are illustrative only, except for the overdraft transfer fee of $1.00 per overdraft and the excessive share transfer fee of $1.00 per item, which are set in the NCUA Standard FCU Bylaws, Art. III, § 4 and § 5(f), respectively.

Appendix C—Official Staff Interpretations

Introduction

1. *Official status.* This commentary is the means by which the staff of the Office of General Counsel of the National Credit Union Administration issues official staff interpretations of Part 707 of the NCUA Rules and Regulations. Good faith compliance with this commentary affords protection from liability under section 271(f) of the Truth in Savings Act (TISA), 12 U.S.C. § 4311.

§ 707.1—Authority, purpose, coverage, and effect on state laws.

(c) Coverage

1. *Foreign applicability.* Part 707 applies to all credit unions that offer share and deposit accounts to residents (including resident aliens) of any state as defined in 707.2(v) and that offer accounts insurable by the National Credit Union Share Insurance Fund (NCUSIF) whether or not such accounts are insured by the NCUSIF. Corporate credit unions designated as such by NCUA under 12 CFR § 704.2 (definition of "corporate credit union") are exempt from part 707.

2. *Persons who advertise accounts.* Persons who advertise accounts are subject to the advertising rules. This includes agent and agented accounts, such as a member who subdivides interests in a jumbo term share certificate account for sale to other parties or among members who form a certificate account investment club. For example, if an agent places an advertisement that offers members an interest in an account at a credit union, the advertising rules apply to the advertisement, whether the account is held by the agent or directly by the member.

3. *Nonautomated credit unions.* Nonautomated credit unions with an asset size of $2 million or less, after subtracting any nonmember deposits, are exempt from TISA and part 707. NCUA defines a "nonautomated credit union" as a credit union without sufficient data processing capability and capacity to establish, operate and maintain a share and loan software system to timely and accurately process all account transactions of all members. The nonautomated credit union exemption is available to all credit unions meeting the asset size and automation standards of this comment, including newly chartered credit unions. If any of the credit unions eligible for this exemption grow to have more than $2 million in assets as of December 31 of any year, the NCUA Board will require such credit unions to comply with TISA and part 707 on January 1 of one year after such credit union loses its exemption eligibility. Similarly, if a credit union becomes sufficiently automated to operate a complete share and loan system, such credit union will be entitled to the same compliance phase-in period.

(d) Effect on state laws

1. *Preemption of state laws/Inconsistent requirements.* State law requirements that are inconsistent with the requirements of TISA and part 707 are preempted to the extent of the inconsistency. A state law is inconsistent if it requires a credit union to make disclosures or take actions that contradict the requirements of the federal law. A state law is also contradictory if it requires the use of the same term to represent a different amount or a different meaning than the federal law, requires the use of a term different from that required in the federal law to describe the same item, or permits a method of calculating dividends or interest on an account different from that required in the federal law.

2. *Preemption determinations.* A credit union, state, or other interested party may request the Board to determine whether a state law requirement is inconsistent with the federal requirements. A request for a determination should be addressed to NCUA's Office of General Counsel, 1775 Duke Street, Alexandria, VA 22314. Written preemption requests should cite (or include a copy of) the allegedly inconsistent state law, demonstrate the inconsistency with TISA and part 707 and the burden on credit unions, and formally request a preemption determination. The Office of General Counsel may provide other interested parties, particularly affected states, an informal opportunity to comment on any request for a preemption determination, unless it finds that such notice and opportunity for comment would be impracticable, unnecessary, or contrary to the public interest. NCUA will publicize any preemption determinations using any means readily at its disposal.

3. *Effect of preemption determinations.* After the Board, through its Office of General Counsel, determines that a state law is inconsistent,

a credit union may not make disclosures using the inconsistent term or take actions relying on the inconsistent law.

4. *Reversal of determination.* The Board reserves the right to reverse a determination for any reason bearing on the coverage or effect of state or federal law.

§ 707.2—Definitions.

(a) Account

1. *Covered accounts.* Examples of accounts subject to the regulation are:

i. Dividend-bearing and interest-bearing accounts.

ii. Non-dividend-bearing and non-interest-bearing accounts.

iii. Accounts opened as a condition of obtaining a credit card.

iv. Escrow accounts with a consumer purpose, such as an account established by a member to escrow rental payments, pending resolution of a dispute with the member's landlord.

v. Accounts held by a parent or custodian for a minor under a state's Uniform Gift to Minors Act (or Uniform Transfers to Minors Act).

vi. Individual retirement accounts (IRAs) and simplified employee pension (SEP) accounts.

vii. Payable-on-Death (POD) or "Totten trust" accounts.

2. *Other accounts.* Examples of accounts not subject to the regulation are:

i. Mortgage escrow accounts for collecting taxes and property insurance premiums.

ii. Accounts established to make periodic disbursements on construction loans.

iii. Trust accounts opened by a trustee pursuant to a formal written trust agreement (not merely declarations of trust on a signature card such as a "Totten trust," or an IRA or SEP account).

iv. Accounts opened by an executor in the name of a decedent's estate.

v. Accounts of individuals operating businesses as sole proprietors.

vi. Certificates of indebtedness. Some credit unions borrow funds from their members through a certificate of indebtedness that sets forth the terms and conditions of the repayment of the borrowing, such as federal credit unions do through 12 CFR § 701.38. Such an account does not represent an account in a credit union and is not covered by part 707.

vii. Unincorporated nonbusiness association accounts.

3. *Other investments.* The term "account" does not apply to these products. Examples of products not covered are:

i. Government securities.

ii. Mutual funds.

iii. Annuities.

iv. Securities or obligations of a credit union.

v. Contractual arrangements such as repurchase agreements, interest rate swaps, and bankers acceptances.

vi. Purchases of U.S. Savings Bonds through a credit union.

vii. Services offered through a group purchasing plan or a credit union service organization (CUSO).

4. *Options.* All dividend-bearing and interest-bearing accounts are either fixed-rate or variable-rate accounts.

5. *Use of synonyms.* Generally, it is not the purpose of part 707 to prohibit specific descriptive terms for accounts. For example, credit unions can use adjectives and trade names to describe accounts such as "Best Share Draft Account," or "Ultra Money Market Share Account." Synonyms for share, share draft, money market share, and term share accounts may be used to describe various types of credit union share and deposit accounts as long as the synonym is accurate and not misleading and, for account disclosures, is used in conjunction with the correct legal term. For example, the following synonyms may be used:

i. The term "checking account" may be used to describe share draft accounts.

ii. The term "money market account" may be used to describe money market share accounts.

iii. The term "savings account" may be used to describe regular share and share accounts.

iv. The terms "share certificate," "certificate account," or "certificate" may be used to describe share certificates and other dividend-bearing term share accounts.

v. However, under no circumstances may a credit union describe a share account as a deposit account, or vice versa. For example, the term "certificate of deposit" or "CD" may not be used to describe share certificates and other dividend-bearing term share accounts. Similarly, the terms "time account" (used in Regulation DD, 12 CFR § 230.2(u)) and "time deposit"

(used in Regulation D, 12 CFR § 204.2(c)) may not be used to describe term share accounts.

(b) *Advertisement*

1. *Covered messages.* Advertisements include commercial messages in visual, oral, or print media that invite, offer, or otherwise announce generally to members and potential members the availability of member accounts such as:

i. Telephone solicitations.

ii. Messages on automated teller machine (ATM) screens (including any printout).

iii. Messages on a computer screen in a credit union's lobby (including any printout) other than a screen viewed solely by the credit union's employee.

iv. Messages in a newspaper, magazine, or promotional flyer or on radio or television.

v. Messages promoting an account that are provided along with information about the member's existing account at a credit union and that promote another account at the credit union (such as account promotional messages on the periodic statement).

2. *Other messages.* Examples of messages that are not advertisements are:

i. Rate sheets published in newspapers, periodicals, or trade journals (unless the credit union or share and deposit broker that offers accounts at the credit union pays a fee to have the information included or otherwise controls publication).

ii. Telephone conversations initiated by a member or potential member about an account.

iii. An in-person discussion with a member about the terms for a specific account.

iv. Information provided to members about their existing accounts, such as on IRA disbursements, notices for automatically renewable term share accounts sent before renewal, or current rates recorded on a voice response machine.

(c) Annual Percentage Yield.

1. *General.* The annual percentage yield (APY) is required for disclosures for new accounts, oral responses to inquiries about rates; disclosures provided upon request; initial disclosures (if the credit union chooses to provide full disclosures instead of the abbreviated notice); notices prior to the renewal of a term share account, if known at the time the notice is sent, and in advertising. The annual percentage yield shows the total amount of dividends for a 365 day period (or a 366 day period for a leap year) on an assumed principal amount based on the dividend rate and frequency of compounding as a percentage of the assumed principal (for accounts such as share or share draft accounts) or for the total amount of dividends over the term of the account for term share accounts. The annual percentage yield assumes the principal amount remains in the account for 365 days (366 days for leap year) or for the term of the account.

2. *How Annual Percentage Yield Differs from Annual Percentage Yield Earned.* The annual percentage yield (APY) differs from the annual percentage yield earned (APYE). The annual percentage yield earned is required for periodic statements only. The annual percentage yield earned shows the total amount of dividends earned for the dividend or statement period as a percent of the actual average daily balance in the member's account. Unlike the annual percentage yield, the annual percentage yield earned is affected by additions and withdrawals during the period. The annual percentage yield and the annual percentage yield earned must be calculated according to the formulas provided in Appendix A to this rule.

(d) Average Daily Balance Method.

1. *General.* One of the two required methods (the daily balance is the other) of determining the balance upon which dividends must be accrued and paid. The average daily balance method requires the application of a periodic rate to the average daily balance in the account for the average daily balance calculation period. The average daily balance is determined by adding the full amount of principal in the account for each day of the period and dividing that figure by the number of days in the period.

(e) Board.

1. *General.* The NCUA Board.

(f) Bonus

1. *General.* Bonuses include items of value offered as incentives to members, such as an offer to pay the final installment deposit for a holiday club account if the final installment is over $10. Bonuses do not include the payment of dividends (including extraordinary dividends), the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, or other consideration aggregating $10 or less per year.

2. *Examples.* The following are examples of bonuses.

i. A credit union offers $25 to potential members for becoming a member and opening

an account. The $25 could be provided by check, cash, or direct deposit.

ii. A credit union offers $25 to a member with only a regular share account to open a share draft account. The $25 could be provided by check, cash, or direct deposit.

iii. A credit union offers a portable radio with a value of $20 to members and potential members for opening a share draft account.

iv. A credit union pays the final installment deposit for a holiday club account if over $10.

3. *Examples not comprising bonuses.* The following are examples of items that are not bonuses:

i. Discount coupons distributed by credit unions for use at restaurants or stores.

ii. A credit union offers $20 to any member if the member is responsible for encouraging a potential member to open an account. The $20 is not a bonus because the $20 is not paid to the individual opening the account. Any item, including cash, given or offered to a third party (that is not a joint member or joint owner in an account being opened) in exchange for a member or potential member opening (or a member renewing or adding to) an account is not a bonus.

iii. A credit union offers $25 to a member if the member can locate his name in the body of a newsletter.

iv. Life savings benefits. Many credit unions offer life savings benefits to beneficiaries of deceased members. Because the benefit accrues to a third party, such life savings plans offered are not bonuses.

v. A credit union offers to pay annual membership dues in a benevolent organization for a class of members.

4. *De minimis rule.* Items with a de minimis value of $10 or less are not bonuses. Credit unions may rely on the valuation standard used by the Internal Revenue Service (IRS) to determine if the value of the item is de minimis. Items required to be reported by the credit union under IRS rules are bonuses under this regulation. Examples of items of de minimis value are:

i. Disability insurance premiums on a share account valued at an amount of $10 or less per year.

ii. Coffee mugs, T-shirts or other merchandise with a market value of $10 or less per year.

5. *Aggregation.* In determining if an item valued at $10 or less is a bonus, credit unions must aggregate per account per calendar year items that may be given to members. In making this determination, credit unions aggregate per account only the market value of items that may be given for a specific promotion. To illustrate, assume a credit union offers in January to give members an item valued at $7 for each calendar quarter during the year that the average account balance in a share draft account exceeds $10,000. The bonus rules are triggered, since members are eligible under the promotion to receive up to $28 during the year. However, the bonus rules are not triggered if an item valued at $7 is offered to members opening a share draft account during the month of January, even though in November the credit union introduces a new promotion that includes, for example, an offer to existing share draft accountholders for an item valued at $8 for maintaining an average balance of $5,000 for the month.

6. *Waiver or reduction of a fee or absorption of expenses.* Bonuses do not include value received by members through the waiver or reduction of fees for credit union-related services (even if the fees waived exceed $10), such as the following:

i. Waiving a safe deposit box rental fee for one year for members who open a new account.

ii. Waiving fees for travelers checks for members, and waiving check and share draft printing fees.

iii. Nondiscriminatorily waiving all fees for a particular class of members, such as seniors or minors.

iv. Discounts on interest rates charged for loans at the credit union.

v. Rebates of loan interest already paid by a member.

vi. Discounts on application fees charged for loans at the credit union.

vii. Packaged, linked, or tied-account services.

7. *Non-dividend membership benefits.* Such benefits are not bonuses because they are sporadic in nature, often difficult to value, and providing non-dividend membership benefits is a long- standing unique credit union practice. (See commentary to § 707.2(r) for examples of such benefits.)

(g) Credit union.

1. *General.* Includes credit unions in the United States, Puerto Rico, Guam, U.S. Virgin Islands, and U.S. territories. Applies to credit unions whether or not the accounts in the credit union are federally, state, privately insured, or uninsured.

(h) Daily balance method.

1. *General.* One of the two required methods (the average daily balance is the other) of determining the balance upon which dividends must be accrued and paid. The daily balance method requires the application of a daily periodic rate to the full amount of principal in the account each day.

(i) Dividend and dividends.

1. *General.* Member savings placed in share accounts are equity investments, and the returns earned on these accounts are dividends. Federal credit unions may only offer dividend-bearing and non-dividend-bearing share accounts. State-chartered credit unions may offer both share and deposit accounts if permitted by state law. State law, including without limitation regulations and official interpretations, will determine if returns earned in accounts in state-chartered credit unions are dividends. Dividends exclude the payment of a bonus or other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, and extraordinary dividends. Dividend-bearing accounts must be either fixed-rate or variable-rate accounts.

2. *Procedure.* Credit unions must follow appropriate law (state law for state-chartered credit unions and federal law for federal credit unions) in determining dividend policies and declaring dividends. Generally, dividends may be viewed as a portion of the available current and undivided earnings of the credit union which is set apart, after required transfers to reserves, by valid act of the board of directors, for distribution among the members. As a matter of legal procedure, members are usually not entitled to dividends until the following steps are completed: (1) the board of the credit union develops a nondiscriminatory dividend policy, by establishing dividend periods, dividend credit determination dates, dividend distribution dates, any associated penalties (if applicable), and the method of dividend computation for each type of share account; (2) the provision for required transfers to reserves are made; (3) sufficient and available prior and/or current earnings are available at the end of the dividend period; (4) the board formally makes a dividend declaration in accordance with the credit union's dividend policy; and (5) dividends must be paid to members by a credit to the appropriate share account, payment by check or share draft, or by a combination of the two methods.

3. *When available.* Credit unions must follow the law of their primary chartering authority to determine when dividends are available. Generally, it is the declaration of the dividend itself which creates the dividend and the member has no right to receive a dividend until it is so declared. The decision of when to declare dividends lies within the official discretion of each credit union's board of directors and cannot be abrogated by contract. An agreement to pay dividends on a share account is generally interpreted not as an obligation to pay the stipulated dividends absolutely and unconditionally, but as an undertaking to pay them out of the earnings when sufficiently accumulated from which dividends in general are properly payable. Generally, "prospective rates" are rates set in good faith in advance of the close of a dividend period, that may be altered if sufficient funds are not available, or in the event of a superseding event, such as a strike, plant closure, significant fluctuation in market rates and/or a significant change in financial structure, natural disaster or emergency that alters the assumptions under which the "prospective rates" were made. It is the intent of TISA that all disclosures be accurate when made, and credit unions are urged to make every effort to ratify disclosed "prospective rates." "Prospective rates" may also be referred to as "projected rates" or similar wording, but not as "estimated rates." (See comment 3(b)-2, prohibiting use of estimates).

4. *Sample dividend resolutions.*

(i) The following resolution may be used where the dividend rates are set after the close of a dividend period.

RESOLUTION OF BOARD OF DIRECTORS FOR THE DECLARATION OF DIVIDENDS

A. I, _____, certify that I am Secretary of _____ Credit Union Board of Directors, and that the following is a correct copy of the resolution for declaring dividends adopted by the _____ Credit Union at a meeting of the Board of Directors duly and properly held on _____, 19____.

This resolution appears in the minutes of this meeting and has not been rescinded or modified.

B. RESOLVED, that

(1) The Board of Directors has developed a nondiscriminatory dividend policy, by establishing dividend periods, dividend credit determination dates, dividend distribution dates, any associated penalties (if applicable), and the method of dividend computation for each type of share account;

(2) The required transfers to reserves have been made; and

(3) Sufficient and available prior and/or current earnings are available at the end of this dividend period.

C. RESOLVED, further, that the Board of Directors now formally makes a dividend declaration in accordance with the Credit Union's dividend policy and authorizes that on _____, 19____, dividends must be paid to members by a credit to the appropriate share account, payment by share draft or by a combination of the two methods.

D. I further certify that the Board of Directors of this Credit Union has, and the time of adoption of this resolution had, full power and lawful authority to adopt the foregoing resolutions and that this resolution revokes any prior resolution.

IN WITNESS WHEREOF, this is my signature and the date on which I signed this Resolution.

_____

Signature

_____

Date

[Attach list of accounts with dividend rates for each type of account.]

(ii) The following resolution may be used where the dividend rates are set before the close of a dividend period.

RESOLUTION OF BOARD OF DIRECTORS FOR THE DECLARATION OF DIVIDENDS

A. I, _____, certify that I am the Secretary of _____ Credit Union, and that the following is a correct copy of the resolution for declaring dividends adopted by the _____ Credit Union at a meeting of the Board of Directors duly and properly held on _____, 19____. This resolution appears in the minutes of that meeting and has not been rescinded or modified.

B. RESOLVED, that the Board of Directors has adopted a nondiscriminatory dividend policy, by establishing dividend periods, dividend credit determination dates, dividend distribution dates, any associated penalties (if applicable) and the method of dividend computation for each type of share account.

C. RESOLVED, that it is the policy and practice of the Board of Directors to meet periodically to establish prospective dividend rates for each type of dividend-bearing share account.

D. RESOLVED, that if the required transfers to reserves have been made and there are sufficient and available prior and/or current earnings available at the end of a dividend period, the officers of the Credit Union are authorized to pay dividends at the rate prospectively established by the Board of Directors for each account for the dividend period. The officers may pay the dividends without any further action of the Board of Directors. The act of paying the dividends shall constitute the declaration of the dividends and shall be a ratification of the prospective dividend rate.

IN WITNESS WHEREOF, this is my signature and the date on which I signed this Resolution.

_____

Signature

_____

Date

[Attach list of accounts with prospective dividend rates for each type of account.]

5. *Referencing.* Except where specifically stated otherwise, use of the term "share" in part 707, as in "share account," also refers to "deposit," as in "deposit account," where appropriate (for interest-bearing or non-interest-bearing deposit accounts at some state-chartered credit unions).

(j) Dividend declaration date.

1. *General.* The importance of the dividend declaration date is to tie the last paid dividend to a certain period of time to place members and potential members on notice that the last paid dividend is different from the next dividend to be paid. In order to achieve this purpose, a credit union may use any of the following methods:

i. "As of 3/15/95" (the date the board of directors last met and declared the last paid dividend).

ii. "As of 3/31/95" (the last day of the last dividend period upon which a dividend has been paid).

iii. "For the period 1/1/95 to 3/31/95" (the last dividend period upon which a dividend has been paid).

iv. "For the first quarter of 1995" (the last dividend period upon which a dividend has been paid).

v. "For April 1995" (the last dividend period upon which a dividend has been paid).

vi. "As of the last dividend declaration date" (the last dividend period upon which a dividend has been paid).

(k) Dividend period.

1. *General.* The dividend period is to be set by a credit union's board of directors for each account type, e.g., regular share, share draft, money market share, and term share. The most common dividend periods are weekly, monthly, quarterly, semi-annually, and annually. Dividend periods need not agree with calendar months, e.g., a monthly dividend period could begin March 15 and end April 14.

(l) Dividend rate.

1. *General.* The dividend rate does not reflect compounding. Compounding is reflected in the "annual percentage yield" definition.

2. *Referencing.* Except where specifically stated otherwise, use of the term "dividend rate" in part 707 also refers to "interest rate," where appropriate (for interest-bearing and non-interest- bearing deposit accounts at some state-chartered credit unions).

(m) Extraordinary dividends.

1. *General.* The definition encompasses all irregularly scheduled and declared dividends, and as dividends, extraordinary dividends are exempt from the "bonus" disclosure requirements. Extraordinary dividends do not have to be disclosed on account disclosures, but the dollar amount of an extraordinary dividend credited to the account during the statement period does have to be separately disclosed on the periodic statement for the dividend period during which the extraordinary dividends are earned. Extraordinary dividends, like ordinary dividends, do not include the payment of a bonus or other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses or non-dividend membership benefits. See comments 2(f) 1 through 7 and 2(i) 1 through 4. Extraordinary dividends may be calculated by any means determined by the board of directors of a credit union and may not be used in the annual percentage yield earned calculation.

2. *Use of synonym.* Extraordinary dividends may be described as "bonus dividends."

(n) Fixed-rate account.

1. *General.* Includes all accounts in which the credit union, by contract, agrees to give at least 30 days advance written notice of decreases in the dividend rate. Thus, credit unions can decrease rates only after providing advance written notice of rate decreases, e.g., a "change-in-terms notice."

(o) Grace period.

1. *General.* A period after maturity of an automatically renewing term share account during which the member may withdraw funds without being assessed a penalty. Use of a "grace period" is discretionary, not mandatory. This definition does not refer to the "grace period" account, which is a synonym for "federal rollback method" or "in by the 10th" accounts, which are prohibited by TISA and part 707.

(p) Interest.

1. *General.* Member savings placed in deposit accounts are debt investments, and the return earned on these accounts is interest. Federal credit unions are not authorized to offer any interest-bearing deposit accounts. State-chartered credit unions may offer both share and deposit accounts if permitted by state law. State law, including without limitation regulations and official interpretations, will determine if returns earned in accounts in state-chartered credit unions are interest. Interest excludes the payment of a bonus or other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, and extraordinary dividends.

2. *Differences between Dividends and Interest.* Generally, dividends are returns on an equity investment (shares); interest is return on a debt investment (deposits). Dividends, in general, are not properly payable until declared at the close of a dividend period; interest, in general, is properly payable daily according to the deposit contract. Dividend rates are prospective until actually declared; interest rates are set according to contract in advance and are earned on that basis. Share accounts establish a member (owner)/credit union (cooperative) relationship; deposit accounts establish a depositor (creditor)/depositary (debtor) relationship.

3. *Referencing.* Except where specifically stated otherwise, use of the terms "dividend" or "dividends" in part 707 also refers to "interest" where appropriate (for interest-bearing and non-interest-bearing deposit accounts at some state-chartered credit unions).

(q) Member

1. *Professional capacity.* Examples of accounts held by a natural person in a professional capacity for another are:

i. Attorney-client trust accounts.

ii. Trust, estate and court-ordered accounts.

iii. Landlord-tenant security accounts.

2. *Other accounts.* Examples of accounts not held in a professional capacity include accounts held by parents for a child under the Uniform Gifts to Minors Act (or Uniform Transfers to Minors Act.

3. *Retirement plans.* IRAs and SEP accounts are member accounts to the extent that funds are invested in accounts subject to the regulation. Keogh accounts, like sole proprietor accounts, are not subject to the regulation.

(r) Non-dividend membership benefits.

1. *General.* Term reflects unique credit union practices that are difficult to value, encourage community spirit, and are not granted in such quantity as to be includable as calculable dividends.

2. *Examples.* Examples include:

i. Food, refreshments, and drawings and raffles at annual meetings, member functions, and branch openings.

ii. Travel club benefits.

iii. Prizes offered at annual meetings, such as U.S. Savings Bonds, a deposit of funds into the winner's account, trips, and other gifts. Such prizes are not bonuses because they are offered as an incentive to increase attendance at the annual meeting, and not to entice members to open, maintain, or renew accounts or increase an account balance.

iv. Life savings benefits.

(s) Passbook Account

1. *Relation to Regulation E.* Passbook accounts include accounts accessed by preauthorized electronic fund transfers to the account (as defined in 12 CFR § 205.2(j)), such as an account credited by direct share and deposit of social security payments. Accounts that permit access by other electronic means are not "passbook accounts," and any statements that are sent four or more times a year must comply with the requirements of 707.6.

(t) Periodic Statement

1. *General.* Periodic statements are not required by part 707. Passbook and term share accounts are exempt from periodic statement requirements.

2. *Examples.* Periodic statements do not include:

i. Additional statements provided solely upon request.

ii. Information provided by computer through home electronic credit union account services.

iii. General service information such as a quarterly newsletter or other correspondence that describes available services and products.

(u) Potential Member.

1. *General.* A potential member is a natural person eligible for membership in a credit union, who has not yet taken the steps necessary to become a member. The term also includes natural person nonmembers eligible to hold accounts in a credit union pursuant to relevant federal or state law.

2. *Verification of eligibility.* It is recommended that credit unions have sound written procedures in place to identify those eligible for membership. If these procedures include verification measures, such as an application process, verification telephone call or letter to an employer or association within the field of membership, witnessing by an existing member, or similar procedure, then the credit union may first verify the membership eligibility of a potential member before providing account disclosures or other information to the potential member. This process of verifying a member's eligibility status, making a recommendation for membership, and providing account disclosures should be completed within 20 calendar days. This period also applies when potential members not on credit union premises request disclosures.

3. *Nonmembers.* Within its sole discretion, the board of directors of a credit union may provide TISA disclosures to nonmembers who are ineligible for membership or to hold an account at the credit union. If disclosures are made to such nonmembers, it is the position of the Board that no civil liability can accrue to the credit union for any errors in such disclosures. (See commentary to 707.3(d)).

(v) State

General. Territories and possessions include American Samoa, Guam, the Mariana Islands, and the Marshall Islands.

(w) Stepped-rate account

1. *General.* Stepped-rate accounts are those accounts in which two or more dividend rates (known at the time the account is opened) will take effect in succeeding periods.

2. *Example.* An example of a stepped-rate account is a one-year term share certificate

account in which a 5.00 percent dividend rate is paid for the first six months, and 5.50 percent for the second six months.

(x) Term share account

1. *Relation to Regulation D.* Regulation D permits, in limited circumstances, the withdrawal of funds without penalty during the first six days after a "time deposit" is opened. (See 12 CFR § 204.2(c)(1)(i).) But the fact that a member makes a withdrawal as permitted by Regulation D does not disqualify the account from being a term share account for purposes of this regulation (such as withdrawals upon the death of the member, or within a "grace period" for automatically renewable term share accounts).

2. *Club accounts.* Club accounts, including Christmas club, holiday club, and vacation club accounts may be either term share or regular share accounts, depending on the terms of the account. Although club accounts typically have a maturity date, they are not term share accounts unless they also require a penalty of at least seven days' dividends for withdrawals during the first six days after the account is opened.

(y) Tiered-rate Account

1. *General.* Tiered-rate accounts are those accounts in which two or more dividend rates are paid on the account and are determined by reference to a specified balance level. Tiered-rate accounts are of two types: Tiering Method A and Tiering Method B. In Tiering Method A accounts, the credit union pays the applicable tiered dividends rate on the entire amount in the account. This method is also known as the "hybrid" or "plateau" tiered-rate account. In Tiering Method B accounts, the credit union does not pay the applicable tiered dividends rate on the entire amount in the account, but only on the portion of the share account balance that falls within each specified tier. This method is also known as the "pure" or "split-rate" tiered-rate account. (See Appendix A, Section I, D.)

2. *Example.* An example of a tiered-rate account is one in which a credit union pays a 5.00 percent dividend rate on balances below $1,000, and 5.50 percent on balances $1,000 and above.

3. *Term share accounts.* Term share accounts that pay different rates based solely on the amount of the initial share and deposit are not tiered-rate accounts.

4. *Minimum balance accounts.* A requirement to maintain a minimum balance to earn dividends does not make an account a tiered-rate account. If dividends are not paid on amounts below a specified balance level, then the account has a minimum balance requirement (required to be disclosed under § 707.4(b)(3)(i)), but the account does not constitute a tiered-rate account. A zero rate (0%) cannot constitute a tier. Minimum balance accounts are single rate accounts with a minimum balance requirement.

(z) Variable-rate account

1. *General.* Includes accounts in which the credit union does not contract to give at least 30 days advance written notice of decreases in the dividend rate. An account meets this definition whether the rate change is determined by reference to an index, by use of a formula, or merely at the discretion of the credit union's board of directors. An account that permits one or more rate adjustments prior to maturity at the member's option, such as a rate relock option, is a variable-rate account.

2. *Differences between fixed-rate and variable-rate accounts.* All accounts must either be fixed-rate or variable-rate accounts. Classifying an account as variable-rate affects credit unions three ways:

i. Additional account disclosures are required (§ 707.4(b)(1)(ii));

ii. Rate decreases are exempted from change-in-terms requirements (§ 707.5(a)(2)(i)); and

iii. Advertising notice required (§ 707.8(c)(1)). Fixed-rate accounts require a contract term obligating the credit union to a 30-day advance, written notice to members before decreasing the dividend rate on the account. Term changes adversely affecting the member and rate decreases cannot take effect until 30 days after such fixed-rate change-in-terms notices are mailed or delivered to members (§ 707.5(a)).

§ 707.3—General disclosure requirements.

(a) Form

1. *General.* All required disclosures (e.g., account disclosures, change-in-terms notices, term share renewal/maturity notices, statement disclosures and advertising disclosures) must be made clearly and conspicuously, in a form the member may retain. Disclosures need be made only as applicable (e.g., disclosures for a non-dividend-bearing account would not include disclosure of annual percentage yield, dividend rate, or other disclosures pertaining to dividend calculations).

2. *Design requirements.* Disclosures must be presented in a format that allows members and potential members to readily understand the terms of their account. Credit unions are not required to use a particular type size or typeface, nor are credit unions required to state any term more conspicuously than any other term. Disclosures may be made:

i. In any order.

ii. In combination with other disclosures or account terms.

iii. In combination with disclosures for other types of accounts, as long as it is clear to members and potential members which disclosures apply to their account.

iv. On more than one page and on the front and reverse sides.

v. By using inserts to a document or filling in blanks.

vi. On more than one document, as long as the documents are provided at the same time.

3. *Consistent terminology.* A credit union must use the same terminology to describe terms or features that are required to be disclosed. For example, if a credit union describes a monthly fee (regardless of account activity), as a "monthly service fee" in account opening disclosures, the periodic statements and change-in-terms notices must use the same terminology so that members and potential members can readily identify the fee.

(b) General

1. *Terms and conditions.* Credit unions are required to have disclosures reflect the terms of the legal obligation between the credit union and a member at the time the member opens the account. This provision does not impose any contract terms or supersede state or other laws that define how the legal obligations between a credit union and its membership are determined.

2. *Specificity of legal obligation.* Credit unions may refer to the calendar month or to roughly equivalent intervals during a calendar year as a "month." Use of estimates is prohibited in TISA disclosures.

3. *Foreign language.* Disclosures may be made in any foreign language, if desired by the board of directors of a credit union. However, disclosures must also be provided in English, upon request.

(c) Relation to Regulation E

1. *General rule.* Compliance with Regulation E (12 CFR part 205) is deemed to satisfy the disclosure requirements of this regulation, such as when:

i. A credit union changes a term that triggers a notice under Regulation E, and the timing and disclosure rules of Regulation E for sending change-in-terms notices.

ii. A member adds an ATM access feature to an account, and the credit union provides disclosures pursuant to Regulation E, including disclosure of fees before the member receives ATM access. (See 12 CFR § 205.7.)

iii. A credit union complying with the timing rules of Regulation E discloses at the same time fees for electronic services (such as balance inquiry fees imposed if the inquiry is made at an ATM) that are required to be disclosed by this regulation, but not by Regulation E.

iv. A credit union relies on Regulation E's rules regarding disclosures of limitations on the frequency and amount of electronic fund transfers, including security-related exceptions. But any limitation on the number of "intra-institutional transfers" to or from the member's other accounts at the credit union during a given time period must be disclosed, even though intra-institutional transfers are exempt from Regulation E.

(d) Multiple members

1. *General.* When an account has multiple natural person member accountholders, delivery of disclosures to any member accountholder or agent authorized by the accountholder satisfies the disclosure requirements of part 707.

(e) Oral response to inquiries

1. *Application of rule.* Credit unions need not provide rate information orally. Disclosures need be made only as appropriate. For example, the requirement to give a telephone number for a member to call about rates for interest-bearing accounts and dividend-bearing term share accounts, would not be necessary for members calling the credit union for information. Also, the disclosure requirements are applicable only to credit union employees and volunteers acting in the ordinary course of credit union business.

2. *Relation to advertising.* The advertising rules do not cover an oral response to a question about rates.

3. *Existing accounts.* This paragraph does not apply to oral responses about rate information for existing term share accounts or accounts not currently offered. For example, if a member holding a one-year term share account requests dividend rate information about the

account during the term, the credit union need not disclose the annual percentage yield, unless the member is calling for rate information under a maturity notice.

(f) Rounding and accuracy rules for rates and yields

(f)(1) Rounding

1. *Permissible rounding.* The annual percentage yield, annual percentage yield earned and dividend rate must be rounded to the nearest one-hundredth of one percentage point (.01%) when disclosed. Examples of permissible rounding are an annual percentage yield calculated to be 5.644%, rounded down and shown as 5.64%; 5.645% would be rounded up and disclosed as 5.65%. For account disclosures, the dividend rate may be expressed to more than two decimal places.

(f)(2) Accuracy

1. *Annual percentage yield and annual percentage yield earned.* The tolerance for annual percentage yield and annual percentage yield earned calculations is designed to accommodate inadvertent errors. Credit unions may not purposely incorporate the one- twentieth of one percentage point (.05%) tolerance into their calculation of yields.

2. *Dividend rate.* There is no tolerance for an inaccuracy in the dividend rate.

§ 707.4—Account disclosures.

(a) Delivery of account disclosures

(a)(1) Account opening

1. *New accounts.* New account disclosures must be provided when:

i. A term share account that does not automatically rollover is renewed by a member.

ii. A member changes the term for a renewable term share account (from a one-year term share account to a six-month term share account, for instance)(see comment 5(b)-5 regarding disclosure alternatives).

iii. A credit union transfers funds from an account to open a new account not at the member's request, unless the credit union previously gave account disclosures and any change-in-terms notices for the new account (e.g., funds in a money market share account are transferred by a credit union to open a new account for the member, such as a share draft account, because the member exceeded transaction limitations on the money market share account).

iv. A credit union accepts a deposit from a member to an account that the credit union had previously deemed to be "closed," under applicable federal or state law, for the purpose of treating accrued, but uncredited, dividends as forfeited dividends. New account numbers are not required by this requirement.

2. *Acquired accounts.* New account disclosures need not be given when a credit union acquires an account through an acquisition of, or merger with, another credit union (but see 707.5(a) regarding advance notice requirements if terms are changed).

3. *Combination disclosures.* New account disclosures need not be given when a member has already received disclosures covering several accounts, and opens a new account properly disclosed by the already received combination disclosures, if the new account is opened within a reasonable amount of time after receipt of the combination disclosures and if the received disclosures and terms are accurate at the time the new account is opened.

(a)(2) Requests

(a)(2)(i)

1. *Inquiries versus requests.* A response to an oral inquiry (by telephone or in person) about rates and yields or fees does not trigger the duty to provide account disclosures. But, when a member asks for written information about an account (whether by telephone, in person, or by other means), the credit union must provide disclosures unless the account is no longer offered to the public.

2. *General requests.* When members or potential members request disclosures about a type of account (a share draft account, for example), a credit union that offers several variations may provide disclosures for any one of them. No disclosures need be made to nonmembers, though a credit union may provide disclosures to nonmembers within its sole discretion.

3. *Timing for response.* Twenty calendar days is a reasonable time for responding to a request for account information that a member does not make in person.

(a)(2)(ii)(A)(2)

1. *Recent rates.* Credit unions comply with this paragraph if they disclose an interest rate (or dividend rate on a dividend- bearing term share account) and annual percentage yield accurate within the seven calendar days preceding the date they send the disclosures.

(a)(2)(ii)(B)

1. *Term.* Describing the maturity of a term share account as "1 year" or "6 months," for example, illustrates a response stating the

maturity of a term share account as a term rather than a date (e.g., "June 1, 1995").

(b) Content of account disclosures

(b)(1) Rate information

(b)(1)(i) Annual percentage yield and dividend rate

1. *Rate disclosures.* In addition to the dividend rate and annual percentage yield, credit unions may disclose a periodic rate corresponding to the dividend rate. No other rate or yield (such as "tax effective yield") is permitted. If the annual percentage yield is the same as the dividend rate, credit unions may disclose a single figure but must use both terms.

2. *Fixed-rate accounts.* For fixed-rate term share accounts paying the opening rate until maturity, credit unions may disclose the period of time the dividend rate will be in effect by stating, or cross-referencing, the maturity date. For other fixed-rate accounts, credit unions may use a date (such as "This rate will be in effect through June 30, 1995") or a period (such as "This rate will be in effect for at least 30 days").

3. *Tiered-rate accounts.* Each dividend rate, along with the corresponding annual percentage yield for each specified balance level (or range of annual percentage yields, if appropriate), must be disclosed for tiered-rate accounts. (See Appendix A, Part I, Paragraph D.)

4. *Stepped-rate accounts.* A single composite annual percentage yield must be disclosed for stepped-rate accounts. (See Appendix A, Part I, Paragraph B.) The dividend rates and the period of time each will be in effect also must be provided. When the initial rate offered for a specified time on a variable-rate account is higher or lower than the rate that would otherwise be paid on the account, the calculation of the annual percentage yield must be made as if for a stepped-rate account. (See Appendix A, Part I, Paragraph C.)

5. *Minimum balance accounts.* If a credit union sets a minimum balance to earn dividends, the credit union may, but need not, state that the annual percentage yield is 0% for those days the balance in the account drops below the minimum balance level when using the daily balance method. Nor is a disclosure of 0% required for credit unions using the average daily balance method, if the member fails to meet the minimum balance required for the average daily balance period.

(b)(1)(ii) Variable rates

(b)(1)(ii)(B)

1. *Determining dividend rates.* To disclose how the dividend rate is determined, credit unions must:

i. Identify the index and specific margin, if the dividend rate is tied to an index.

ii. State that rate changes are within the credit union's discretion, if the credit union does not tie changes to an index.

(b)(1)(ii)(C).

1. *Frequency of rate changes.* A credit union reserving the right to change rates at its discretion must state the fact that rates may change at any time.

(b)(1)(ii)(D)

1. *Limitations.* A floor or ceiling on rates or on the amount the rate may decrease or increase during any time period must be disclosed. Credit unions need not disclose the absence of limitations on rate changes.

(b)(2) Compounding and crediting

(b)(2)(i) Frequency

1. *General.* Descriptions such as "quarterly" or "monthly" are sufficient. Irregular crediting and compounding periods, such as if a cycle is cut short at year end for tax reporting purposes, need not be disclosed.

2. *Dividend period.* For dividend-bearing accounts, the dividend period must be disclosed. (A specific example must also be given, see Appendix B, B-1(c).) The dividend period for term share accounts generally may be disclosed as the account's term (e.g., two years).

(b)(2)(ii) Effect of closing an account

1. *Deeming an account closed.* A credit union may, subject to state or other law, provide in account contracts the actions by members that will be treated as closing the account and that will result in the forfeiture of accrued but uncredited dividends. An example is the withdrawal of all funds from the account prior to the date dividends are credited. Credit unions are cautioned that bylaw requirements may prevent a credit union from deeming a member's account closed until certain time periods are extinguished if funds remain in a member's account. *NCUA Standard FCU Bylaws,* Art. III, section 3 (members have at least six months to replenish membership share before membership terminates and account is deemed closed). Such bylaw requirements may not be overridden without proper agency approval.

(b)(3) Balance information

(b)(3)(i) Minimum balance requirements

1. *Par value.* Credit unions must disclose any minimum balance required to open the

account, to avoid the imposition of a fee, or to obtain the annual percentage yield. Since members cannot generally maintain any accounts until the par value of the membership share is paid in full, this section requires that credit unions disclose the par value of a share necessary to become a member and maintain accounts at the credit union. The par value of a share and the minimum balance requirement do not have to be the same amount (e.g., a credit union may have a $5 par value for a membership share, in order for accounts to be opened and maintained, and a $100 minimum balance requirement, in order for the account to earn dividends).

2. *Disclosures.* The explanation of minimum balance computation methods may be combined with the balance computation method disclosures (§ 707.4(b)(3)(ii)) if they are the same. If a credit union uses different cycles for determining minimum balance requirements for purposes of assessing fees and for paying dividends, the credit union must disclose the specific cycle or time period used for each purpose (e.g., use of a midmonth statement cycle for determining dividends, and use of a calendar month cycle for determining fees). Credit unions may assess fees by using any method. If fees on one account are tied to the balance in another account, such provision must be explained (e.g., if share draft fees are tied to a minimum balance in the regular share account (or a combination of the share draft and regular share accounts), the share draft account must explain that fact and how the balance in the regular share account (or both accounts) is determined). The fee need not be disclosed in the account disclosures if the fee is not imposed on that account.

(b)(3)(ii) Balance computation method

1. *Methods and periods.* Credit unions may use different methods or periods to calculate minimum balances for purposes of imposing a fee (the daily balance for a calendar month, for example) and accruing dividends (the average daily balance for a statement period, for example). Each method and corresponding period must be disclosed.

(b)(3)(iii) When dividends begin to accrue

1. *Additional information.* Credit unions must include a statement as to when dividends begin to accrue for noncash deposits. Credit unions may disclose additional information such as the time of day after which deposits are treated as having been received the following business day, and may use additional descriptive terms such as "ledger" or "collected" balances to disclose when dividends begin to accrue. Under the ledger balance method, dividends begin to accrue on the day of deposit. Under the collected balance method, dividends begin to accrue when provisional credit is received for the item deposited.

(b)(4) Fees

1. *Types of fees.* Fees related to the routine use of an account must be disclosed. The following are types of fees that must be disclosed in connection with an account:

i. Maintenance fees, such as monthly service fees.

ii. Fees related to share deposits or withdrawals.

iii. Fees for special services, such as stop payment fees, fees for balance inquiries or verification of shares and deposits, fees associated with checks returned unpaid, fees for regularly sending to members share drafts that otherwise would be held by the credit union, and overdraft line of credit access fees (if charged against the share account).

iv. Fees to open or to close an account.

v. Fees imposed upon dormant or inactive accounts.

2. *Other fees.* Credit unions need not disclose fees such as the following:

i. Fees for services offered to members and nonmembers alike, such as fees for certain travelers checks, for wire transfers and automated clearinghouse (ACH) transfers, to process credit card cash advances, or to handle U.S. Savings Bond redemption (even if different amounts are charged to members and nonmembers).

ii. Incidental fees, such as fees associated with state escheat laws, garnishment or attorneys fees, to change names on an account, to generate a midcycle periodic statement, to wrap loose coins, for photocopying for statements returned to the credit union because of a wrong address, and locator fees.

3. *Amount of fees.* Credit unions are cautioned that merely providing fee information in an account disclosure may not be sufficient to gain the legal right to impose the fee involved under applicable law. Credit unions must state the amount and conditions under which a fee may be imposed. Naming and describing the fee typically satisfies this requirement. Some examples are:

i. "$4.00 monthly service fee".

ii. "$7.00 and up" or "fee depends on style of checks ordered" for check printing fees.

4. *Tied-accounts.* Credit unions must state if fees that may be assessed against an account are tied to other accounts at the credit union. For example, if a credit union ties the fees payable on a share draft account to balances held in the share draft account and in a regular share account, the share draft account disclosures must state that fact and explain how the fee is determined.

5. *Regulation E statements.* Some fees are required to be disclosed under both Regulation E (12 CFR §205.7) and part 707. If such fees, such as ATM transaction fees, are disclosed on a Regulation E statement, they need not be disclosed again on a periodic statement required under part 707.

(b)(5) Transaction limitations

1. *General rule.* Examples of limitations on the number or dollar amount of share deposits or withdrawals that credit unions must disclose are:

i. Limits on the number of share drafts or checks that may be written on an account for a given time period.

ii. Limits on withdrawals or share deposits during the term of a term share account.

iii. Limitations required by Regulation D, such as the number of withdrawals permitted from money market share accounts by check to third parties each month (credit unions need not disclose reservation of right to require a notice for withdrawals from accounts required by federal or state law).

(b)(6) Features of term share accounts

(b)(6)(i) Time requirements

1. "*Callable*" term share accounts. In addition to the maturity date, credit unions must state the date or the circumstances under which the credit union may redeem a term share account at the credit union's option (a "callable" term share account).

(b)(6)(ii) Early withdrawal penalties

1. *General.* The term "penalty" may, but need not, be used to describe the loss that may be incurred by members for early withdrawal of funds from term share accounts.

2. *Examples.* Examples of early withdrawal penalties are:

i. Monetary penalties, such as a specific dollar amount (e.g., "$10.00") or a specific days' worth of dividends (e.g., "seven days' dividends plus accrued but uncredited dividends, but only if the account is closed").

ii. Adverse changes to terms such as the lowering of the dividend rate, annual percentage yield, or reducing the compounding or crediting frequency for funds remaining in shares or on deposit.

iii. Reclamation of bonuses

3. *Relation to rules for IRAs or similar plans.* Penalties imposed by the Internal Revenue Code for certain withdrawals from IRAs or similar pension or savings plans are not early withdrawal penalties for purposes of this regulation.

4. *Disclosing penalties.* Penalties may be stated in months, whether credit unions assess the penalty using the actual number of days during the period or using another method such as a number of days that occurs in any actual sequence of the total calendar months involved. For example, stating "one month's dividends" is permissible, whether the credit union assesses 30 days' dividends during the month of April, or selects a time period between 28 and 31 days for calculating the dividends for all early withdrawals regardless of when the penalty is assessed.

(b)(6)(iv) Renewal policies

1. *Rollover term share accounts.* Credit unions are not required to provide a grace period, to pay dividends during the grace period, or to disclose whether or not dividends will be paid during the grace period. Credit unions offering a grace period on term share accounts must give the length of the grace period. Commentary, Appendix B, Model Clauses, B-1(i)(iv).

2. *Nonrollover term share accounts.* Credit unions that pay dividends on funds following the maturity of term share accounts that do not renew automatically need not state the rate (or annual percentage yield) that may be paid.

(b)(7) Bonuses

1. *General.* Credit unions are required to state the amount and type of bonus, and disclose any minimum balance or time requirement to obtain the bonus and when the bonus will be provided. If the minimum balance or time requirement is otherwise required to be disclosed, credit unions need not duplicate the disclosure for purposes of this paragraph.

(b)(8) Nature of dividends

1. *General.* Dividends are not payable until declared and unless sufficient current and undivided earnings are available after required transfers to reserves at the close of a dividend

period. A disclosure explaining dividends educates members and protects credit unions in the event that a prospective dividend cannot be paid, or is not properly payable. This disclosure is required for all dividend-bearing share accounts. Term share accounts need not include a statement regarding the nature of dividends.

2. *State-chartered credit unions with interest-bearing deposit accounts.* State law controls the nature of accounts (i.e., whether an account is a share account or a deposit account). If a member of a state-chartered credit union is opening only an interest-bearing deposit account, or is requesting account disclosures only for an interest-bearing deposit account (if state law requires the depositor to hold a share account), the disclosures must generally include the following information on any dividend-bearing share portion of the account (e.g., membership share): the par value of a share; a statement that the portion of the deposit that represents the par value of the membership share will earn dividends; and that dividends are paid from current income and available earnings after required transfers to reserves. Further additional disclosures, such as a separate dividend rate and annual percentage yield for the membership share, are not required (if the additional disclosures would agree with the remainder of the account which is invested in an interest-bearing deposit).

(c) Notice to existing accountholders

1. *General.* Only members who receive periodic statements (provided regularly at least four times per year) and who hold accounts of the type offered by the credit union as of the compliance date of part 707 (generally January 1, 1995) must receive the notice. If following receipt of the notice members request disclosures, credit unions have twenty calendar days from receipt of the request to provide the disclosures. Rate and annual percentage yield information in such disclosures must conform to that required for disclosures upon request. As an alternative to including the notice in or on the periodic statement, the final rule permits credit unions to send the account disclosures themselves, as long as they are sent at the same time as the periodic statement (the disclosures may be mailed either with the periodic statement or separately).

2. *Form of the notice.* The notice may be included on the periodic statement, in a member newsletter, or on a statement stuffer or other insert, if it is clear and conspicuous. The notice cannot be sent in a separate mailing from the periodic statement.

3. *Timing.* The notice may accompany the first periodic statement after the compliance date for part 707, or the periodic statement for the first cycle beginning after that date. For example, a credit union's statement cycle is December 15, 1994—January 14, 1995. The statement is mailed on January 15. The next cycle is January 15, 1995 through February 14, 1995, and the statement for that cycle is mailed on February 15. The credit union may provide the notice either on or with the January 15 statement or on or with the February 15 statement, as it covers the first cycle after January 1, 1995.

4. *Early compliance.* Credit unions that provide the notice to existing members prior to the compliance date of part 707, must be prepared to provide accurate and timely disclosures when, following receipt of the notice, members ask for account disclosures. Such disclosures must be provided even if they are requested before the compliance date of part 707. Credit unions who provide early notice to existing members need to comply with other aspects of part 707, but need not provide disclosures already provided in compliance with part 707.

§ 707.5—Subsequent disclosures.

(a) Change in terms

(a)(1) Advance notice required

1. *Form of notice.* Credit unions may provide a change-in-term notice on or with a regular periodic statement or in another mailing (such as a highlighted portion of a newsletter or statement stuffer insert). If a credit union provides notice through revised account disclosures, the changed term must be highlighted in some manner. For example, credit unions may state that a particular fee has been changed (also specifying the new amount) or use an accompanying letter that refers to the changed term. Credit unions are cautioned that unless credit unions have reserved the right to change terms in the account agreement or disclosures, a change-in-terms notice may not be sufficient to amend the terms under applicable law.

2. *Effective date.* An example of language for disclosing the effective date of a change is: "As of May 11, 1995."

3. *Terms that change upon the occurrence of an event.* A credit union offering terms that will automatically change upon the occurrence of a stated event need not send an advance notice of

the change provided the credit union fully describes the conditions of the change in the account opening disclosures (and sends any change-in-term notices regardless of whether the changed term affects that member's account at that time).

4. *Examples.* Examples of changes not requiring an advance change-in-terms notice are:

i. The termination of employment for employee-members for whom account maintenance or activity fees were waived during their employment by the credit union.

ii. The expiration of one year in a promotion described in the account opening disclosures to "waive $4.00 monthly service charges for one year".

(a)(2) No notice required

(a)(2)(ii) Check printing fees

1. *Increase in fees.* A notice is not required for an increase in fees for printing share drafts (or deposit and withdrawal slips) even if the credit union adds some amount to the price charged by the vendor.

(b) Notice before maturity for term share accounts longer than one month that renew automatically

1. *Maturity dates on nonbusiness days.* In determining the term of a term share account, credit unions may disregard the fact that the term will be extended beyond the disclosed number of days if the maturity date falls on a nonbusiness day. For example, a holiday or weekend may cause a "one-year" term share account to extend beyond 365 days (or 366, in a leap year), or a "one-month" term share account to extend beyond 31 days.

2. *Disclosing when rates will be determined.* Ways to disclose when the annual percentage yield will be available include the use of:

i. A specific date, such as "October 28".

ii. A date that is easily discernible, such as "the Tuesday prior to the maturity date stated on the notice" or "as of the maturity date stated on this notice".

3. *Alternative timing rule.* Under the alternative timing rule, a credit union that offers a 10-day grace period would have to provide the disclosures at least 10 calendar days prior to the scheduled maturity date.

4. *Club accounts.* If members have agreed to the transfer of payments from another account to a club term share account for the next club period, the credit union must comply with the requirements for automatically renewable term share accounts—even though members may withdraw funds from the club account at the end of the current club period.

5. *Renewal of a term share account.* In the case of a change-in- terms that becomes effective if a rollover term share account is subsequently renewed:

i. If the change is initiated by the credit union, the disclosure requirements of this paragraph apply. (Paragraph 707.5(a) applies if the change becomes effective prior to the maturity of the existing term share account.)

ii. If the change is initiated by the member, the account opening disclosure requirements of § 707.4(b) apply. (If the notice required by this paragraph has been provided, credit unions may give new account disclosures or disclosures that reflect the new term.)

6. *Example.* If a member receives a notice prior to maturity on a one-year term share account and requests a rollover to a six- month account, the credit union must provide either account opening disclosures including the new maturity date or, if all other terms previously disclosed in the prematurity notice remain the same, only the new maturity date.

(b)(1) Maturities of longer than one year

1. *Highlighting changed terms.* Credit unions need not highlight terms that have changed since the last account disclosures were provided.

(c) Notice before maturity for term share accounts longer than one year that do not renew automatically

1. *Subsequent account.* When funds are transferred following maturity of a nonrollover term share account, credit unions need not provide account disclosures unless a new account is established.

§ 707.6—Periodic statement disclosures.

(a) Rule When Statement and Crediting Periods Vary

1. *General.* Credit unions are not required to provide periodic statements. If they provide periodic statements, disclosures need only be furnished to the extent applicable. For example, if no dividends are earned for a statement period, credit unions need not state that fact. Or, credit unions may disclose "$0" dividends earned and "0%" annual percentage yield earned.

2. *Regulation E interim statements.* When a credit union provides regular quarterly statements, and in addition provides a monthly

interim statement to comply with Regulation E, the interim statement need not comply with this section unless it states dividend or rate information. (See 12 CFR § 205.9.) For credit unions that choose not to treat Regulation E activity statements as part 707 periodic statements, the quarterly periodic statement must reflect the annual percentage yield earned and dividends earned for the full quarter. However, credit unions choosing this option need not redisclose fees already disclosed on an interim Regulation E activity statement on the quarterly periodic statement. For credit unions that choose to treat Regulation E activity statements as part 707 periodic statements, the Regulation E statement must meet all part 707 requirements.

3. *Combined statements.* Credit unions may provide certain information about an account (such as a money market share account or regular share account) on the periodic statement for another account (such as a share draft account) without triggering the disclosures required by this section, as long as:

i. The information is limited to information such as the account number, the type of account, balance information, accountholders' names, and social security or tax identification number; and.

ii. The credit union also provides members a periodic statement complying with this section for the account (the money market share account or regular share account, in the example).

4. *Other information.* Additional information that may be given on or with a periodic statement, includes:

i. Dividend rates and corresponding periodic rates to the dividend rate applied to balances during the statement period.

ii. The dollar amount of dividends earned year-to-date.

iii. Bonuses paid (or any de minimis consideration of $10 or less).

iv. Fees for other products, such as safe deposit boxes.

v. Accounts not covered by the periodic statement disclosure requirements (passbook and term share accounts) may disclose any information on the statement related to such accounts, so long as such information is accurate and not misleading.

5. *When statement and crediting periods vary.* This rule permits credit unions, on dividend-bearing share accounts, to report the annual percentage yield earned and the amount of dividends earned on a statement other than on each periodic statement when the dividend period does not agree with, varies from, or is different than, the statement period. For dividend- bearing share accounts, credit unions may disclose the required information either upon each periodic statement, or on the statement on which dividends are actually earned (credited or posted) to the member's account. In addition, for accounts using the average daily balance method of calculating dividends, when the average daily balance period and the statement periods do not agree, vary or are different, credit unions may also report annual percentage yield earned and the dollar amount of dividends earned on the periodic statement on which the dividends or interest is earned. For example, if a credit union has quarterly dividend periods, or uses a quarterly average daily balance on an account, the first two monthly statements may not state annual percentage yield earned and dividends earned figures; the third "monthly" statement will reflect the dividends earned and the annual percentage yield earned for the entire quarter. The fees imposed disclosure must be given on the periodic statement on which they are imposed.

6. *Length of the period.* Credit unions must disclose the length of both the dividend period (or average daily balance calculation period) and the statement period. For example, a statement could disclose a statement period of April 16 through May 15 and further state that "the dividends earned and the annual percentage yield earned are based on your dividend period (or average daily balance) for the period April 1 through April 30."

7. *Dividend period more frequent than statement period.* Credit unions that calculate dividends on a monthly basis, but send statements on a quarterly basis, may disclose a single dividend (and annual percentage yield earned) figure. Alternatively, a credit union may disclose three dividends earned and three annual percentage yield earned figures, one for each month in the quarter, as long as the credit union states the number of days (or beginning and ending date) in each dividend period if it varies from the statement period.

8. *Additional voluntary disclosures.* For credit unions not disclosing the annual percentage yield earned and dividends earned on all periodic statements, credit unions may place a notice on statements without dividends and annual percentage yield earned figures, that the

annual percentage yield earned and dollar amount of dividends earned will appear on the first statement at the close of the dividend (or average daily balance) period, or similar wording. Credit unions may also choose to include a telephone number to call for interim information, if desired by a member.

(b) Statement Disclosures

(b)(1) Annual percentage yield earned

1. *Ledger and collected balances.* Credit unions that accrue interest using the collected balance method may use either the ledger or collected balance methods to determine the balance used to determine the annual percentage yield earned. Ledger balance means the record of the balance in a member's account, as per the credit union's records. (The ledger balance may reflect additions and deposits for which the credit union has not yet received final payment). Collected balance means the record of balance in a member's account reflecting collected funds, that is, cash or checks deposited in the credit union which have been presented for payment and for which payment has actually been received. (See Regulation CC, 12 CFR § 229.14).

(b)(2) Amount of dividends or interest

1. *Definition of earned.* The term "earned" is defined to include dividends and interest either "accrued" or "paid and credited." Credit unions may use either the "ledger" or the "collected" balance for either option. (See 707.6(b)(1)1 and 707.7(c)(2) of the Appendix.)

2. *Accrued interest.* Credit unions must state the amount of interest that accrued during the statement period, even if it was not credited.

3. *Terminology.* In disclosing dividends earned for the period, credit unions must use the term "dividends" or terminology such as:

"Dividends paid," to describe dividends that have been credited;

"Dividends accrued," to indicate that dividends are not yet credited.

4. *Closed accounts.* If a member closes an account between crediting periods and forfeits accrued dividends, the credit union may not show any figures for "dividends earned" or annual percentage yield earned for the period (other than zero, at the credit union's option).

5. *Extraordinary dividends.* Extraordinary dividends are not a component of the annual percentage yield earned or the dividend rate, but are an addition to the member's account. The dollar amount of the extraordinary dividends paid, denoted as a separate, identified figure, must be disclosed on the periodic statement on which the extraordinary dividends are earned. A credit union may also disclose information regarding the calculation of the extraordinary dividends, and additional annual percentage yield earned and dividend rate figures taking into account the extraordinary dividend, so long as such information is accurate and not misleading.

(b)(3) Fees imposed

1. *General.* Periodic statements must state fees disclosed under 707.4(b) that were debited to the account during the statement period, even if assessed for an earlier period.

2. *Itemizing fees by type.* In itemizing fees imposed more than once in the period, credit unions may group fees if they are the same type. But, the description must make clear that the dollar figure represents more than a single fee, for example, "total fees for checks written this period." Examples of fees that may not be grouped together are:

i. Monthly maintenance with excess activity fees.

ii. "Transfer" fees, if different dollar amounts are imposed—such as $.50 for share deposits and $1.00 for withdrawals.

iii. Fees for electronic fund transfers with fees for other services, such as balance inquiry or maintenance fees.

3. *Identifying fees.* Statement details must enable the member to identify the specific fee. For example:

i. Credit unions may use a code to identify a particular fee if the code is explained on the periodic statement or in documents accompanying the statement.

ii. Credit unions using debit slips may disclose the date the fee was debited on the periodic statement and show the amount and type of fee on the dated debit slip.

4. *Relation to Regulation E.* Disclosure of fees in compliance with Regulation E complies with this section for fees related to electronic fund transfers (for example, totaling all electronic funds transfer fees in a single figure).

(b)(4) Length of period

1. *General.* Credit unions providing the beginning and ending dates of the period must make clear whether both dates are included in the period. For example, stating "April 1 through April 30" would clearly indicate that both April 1 and April 30 are included in the period.

2. *Opening or closing an account mid-cycle.* If an account is opened or closed during the period for which a statement is sent, credit unions must calculate the annual percentage yield earned based on account balances for each day the account was open.

§ 707.7—Payment of dividends.

(a) Permissible methods

1. *Prohibited calculation methods.* Calculation methods that do not comply with the requirement to pay dividends on the full amount of principal in the account each day include:

i. The "rollback" method, also known as the "grace period" or "in by the 10th" method, where credit unions pay dividends on the lowest balance in the account for the period.

ii. The "increments of par value" method, where credit unions only pay dividends on full shares in an account, e.g., a credit union with $5 par value shares pays dividends on $20 of a $24 account balance.

iii. The "ending balance" method, where credit unions pay dividends on the balance in the account at the end of the period.

iv. The "investable balance" method, where credit unions pay dividends on a percentage of the balance, excluding an amount credit unions set aside for reserve requirements.

v. The "low balance" method, where credit unions pay dividends on the lowest balance in the account for any day in that period.

2. *Use of 365-day basis.* Credit unions may apply a daily periodic rate that is greater than 1/365 of the dividend rate—such as 1/360 of the dividend rate—as long as it is applied 365 days a year.

3. *Periodic dividend payments.* A credit union can pay dividends each day on the account and still make uniform dividend payments. For example, for a one-year term share account, a credit union could make monthly dividend payments that are equal to 1/12 of the amount of dividends that will be earned for a 365-day period (or 11 uniform monthly payments—each equal to roughly 1/12 of the total amount of dividends—and one payment that accounts for the remainder of the total amount of dividends earned for the period).

4. *Leap year.* Credit unions may apply a daily rate of 1/366 or 1/365 of the dividend rate for 366 days in a leap year, if the account will earn dividends for February 29.

5. *Maturity of term share accounts.* Credit unions are not required to pay dividends after term share accounts mature. Examples include:

i. During any grace period offered by a credit union for an automatically renewable term share account, if the member decides during that period not to renew the account.

ii. Following the maturity of nonrollover term share accounts.

iii. When the maturity date falls on a holiday, and the member must wait until the next business day to obtain the funds.

6. *Dormant accounts.* Credit unions must pay dividends on funds in an account, even if inactivity or the infrequency of transactions would permit the credit union to consider the account to be "inactive" or "dormant" (or similar status) as defined by state or other law or the account contract.

7. *Insufficient funds.* Credit unions are not required to pay dividends on checks or share drafts deposited to a member's account that are returned for insufficient funds. If a credit union accrues dividends on a check that it later determines is not good, it may deduct from the accrued dividends any dividends attributed to the proceeds of the returned check. If dividends have already been credited before the credit union determines the item has insufficient funds, the credit union may deduct the amount of the check and associated dividends from the account balance. The amount deducted will not be reflected in the dividend amount and annual percentage yield earned reported for the next period.

8. *Account drawn below par value of a share.* If a member draws his or her account below the par value of a share, dividends would continue to accrue on the account so long as any minimum balance requirement is met. However, under the NCUA Standard FCU Bylaws, if a member who reduces his or her share balance below the value of a par value share and does not increase the balance within at least six months, the credit union may terminate the member's membership. State-chartered credit unions may have similar termination provisions.

(a)(2) Determination of minimum balance to earn dividends

1. *General.* Credit unions may set minimum balance requirements that must be met in order to earn dividends. However, credit unions must use the same method to determine a minimum balance required to earn dividends as they use to determine the balance upon which dividends

will accrue and pay. For example, a credit union that calculates dividends on the daily balance method must use the daily balance method to determine if the minimum balance to earn dividends has been met. Similarly, a credit union that calculates dividends on the average daily balance method must use the average daily balance method to determine if the minimum to earn dividends has been met. Credit unions may have a par value of a share that is different from the minimum balance requirement to earn dividends. (See commentary to § 707.4(b)(3)(i)).

2. *Daily balance accounts.* Credit unions that require a minimum balance to earn dividends may choose not to pay dividends for days when the balance drops below the required minimum balance if they use the daily balance method to calculate dividends. For example, a credit union could set a minimum daily balance level of $200 and pay dividends only those days the $200 daily balance is maintained.

3. *Average daily balance accounts.* Credit unions that require a minimum balance to earn dividends may choose not to pay dividends for the average daily balance calculation period in which the average daily balance drops below the required minimum, if they use the average daily balance method to calculate dividends. For example, a credit union could set a minimum average daily balance level of $200 and pay dividends only if the $200 average daily balance is met for the calculation period.

4. *Beneficial method.* Credit unions may not require members to maintain both a minimum daily balance and a minimum average daily balance to earn dividends, such as by requiring the member to maintain a $500 daily balance and a prescribed average daily balance (whether higher or lower). But a credit union could offer a minimum balance to earn dividends that includes an additional method that is "unequivocally beneficial" to the member such as the following:

i. A credit union using the daily balance method to calculate dividends and requiring a $500 minimum daily balance could choose to pay dividends on the account (for those days the minimum balance is not met) as long as the member maintained an average daily balance throughout the month of $400.

ii. A credit union using the average daily balance method to calculate dividends and requiring a $400 minimum average daily balance could choose to pay dividends on the account as long as the member maintained a daily balance of $500 for at least half of the days in the period.

iii. A credit union using either the daily balance method or average daily balance method to calculate dividends that requires: (A) a $500 daily balance; or (B) a $400 average daily balance to pay dividends on the account.

5. *Paying on full balance.* Credit unions must pay dividends on the full balance in the account that meets the required minimum balance. For example, if $300 is the minimum daily balance required to earn dividends, and a member deposits $500, the credit union must pay the stated dividend rate on the full $500 and not just on $200.

6. *Negative balances prohibited.* Credit unions must treat a negative account balance as zero to determine:

i. The daily or average daily balance on which dividends will be paid.

ii. Whether any minimum balance to earn dividends is met (See commentary to Appendix A, Part II, which prohibits credit unions from using negative balances in calculating the dividends figure for the annual percentage yield earned.)

7. *Club accounts.* Credit unions offering club accounts (such as a "holiday" or "vacation" club accounts) cannot impose a minimum balance requirement for dividends based on the total number or dollar amount of payments required under the club plan. For example, if a plan calls for $10 weekly payments for 50 weeks, the credit union cannot set a $500 minimum balance and then pay only if the member makes all 50 payments.

8. *Minimum balances not affecting dividends.* Credit unions may use the daily balance, average daily balance, or other computation method to calculate minimum balance requirements not involving the payment of dividends—such as to compute minimum balances for assessing fees.

(b) Compounding and crediting policies

1. *General.* Credit unions choosing to compound dividends may compound or credit dividends annually, semi-annually, quarterly, monthly, daily, continuously, or on any other basis.

2. *Withdrawals prior to crediting date.* If members withdraw funds (without closing the account), prior to a scheduled crediting date, credit unions may delay paying the accrued dividends on the withdrawn amount until the

scheduled crediting date, but may not avoid paying dividends.

3. *Closed accounts.* Subject to state or other law, a credit union may choose not to pay accrued dividends if members close an account prior to the date accrued dividends are credited, as long as the credit union has disclosed that fact. If accrued dividends are paid, accrued dividends must be paid on funds up until the account is closed or the account is deemed closed. For example, if an account is closed on a Tuesday, accrued dividends on the funds through Monday would be paid. Whether (and the conditions under which) credit unions are permitted to deem an account closed by a member is determined by state or other law, if any. Credit unions are cautioned that bylaw requirements may prevent a credit union from deeming a member's account closed until certain time periods are extinguished. (See NCUA Standard FCU Bylaws, Art. III, 3 (members have at least 6 months to replenish membership share before membership can terminate and the account is deemed closed). Such bylaw requirements may not be overridden without proper agency approval.)

(c) Date dividends begin to accrue

1. *Relation to Regulation CC.* Credit unions may rely on the Expedited Funds Availability Act (EFAA) and Regulation CC (12 CFR part 229) to determine, for example, when a deposit is considered made for purposes of dividend accrual, or when dividends need not be paid on funds because a deposited check is later returned unpaid.

2. *Ledger and collected balances.* Credit unions may calculate dividends by using a "ledger" balance or "collected" balance method, as long as the crediting requirements of the EFAA are met (12 CFR § 229.14).

3. *Withdrawal of principal.* Credit unions must accrue dividends on funds until the funds are withdrawn from the account. For example, if a check is debited to an account on a Tuesday, the credit union must accrue dividends on those funds through Monday.

§ 707.8—Advertising.

(a) Misleading or inaccurate advertisements

1. *General.* All advertisements are subject to the rule against misleading or inaccurate advertisements, even though the disclosures applicable to various media differ. The word "profit" may be used when referring to dividend-bearing share accounts, as it reflects the nature of dividends. The word "profit" may not be used when referring to interest-bearing deposit accounts.

2. *Indoor signs.* An indoor sign advertising an annual percentage yield is not misleading or inaccurate if:

i. For a tiered-rate account, it also provides the upper and lower dollar amounts of the tier corresponding to the advertised annual percentage yield.

ii. For a term share account, it also provides the term required to obtain the advertised annual percentage yield.

3. *"Free" or "no cost" accounts.* For purposes of determining whether an account can be advertised as "free" or "no cost," maintenance and activity fees include:

i. Any fee imposed if a minimum balance requirement is not met, or if the member exceeds a specified number of transactions.

ii. Transaction and service fees that members reasonably expect to be imposed on an account on a regular basis (See comments 4(b)(4)-1 and 2.)

iii. A flat fee, such as a monthly service fee.

iv. Fees imposed to deposit, withdraw or transfer funds, including per-check or per-transaction charges (for example, $.25 for each withdrawal, whether by check, or in person).

4. *Other fees.* Examples of fees that are not maintenance or activity fees include:

i. Fees that are not required to be disclosed under § 707.4(b)(4).

ii. Check printing fees of any type.

iii. Fees for obtaining copies of checks, whether or not the original checks have been truncated or returned to the member periodically.

iv. Balance inquiry fees.

v. Fees assessed against a dormant account.

vi. Fees for using an ATM.

vii. Fees for electronic transfer services that are not required to obtain an account, such as preauthorized transfers or home electronic credit union services.

viii. Stop payment fees and fees for share drafts or checks returned unpaid.

5. *Similar terms.* An advertisement may not use a term such as "fees waived" if a maintenance or activity fee may be imposed because it is similar to the terms "free" or "no cost."

6. *Specific account services.* Credit unions may advertise a specific account service or fea-

ture as free as long as no fee is imposed for that service or feature. For example, credit unions offering an account that is free of deposit or withdrawal fees could advertise that fact, as long as the advertisement does not mislead members by implying that the account is free and that no other fee (a monthly service fee, for example) may be charged.

7. *Free for limited time.* If an account (or a specific account service) is free only for a limited period of time—for example, for one year following the account opening—the account (or service) may be advertised as free as long as the time period is stated.

8. *Conditions not related to share accounts.* Credit unions may advertise accounts as "free" for members that meet conditions not related to share accounts, such as the member's age. For example, credit unions may advertise a share draft account as "free for persons over 65 years old," even though a maintenance or activity fee may be assessed on accounts held by members that are 65 or younger.

(b) Permissible rates

1. *Tiered-rate accounts.* An advertisement for a tiered-rate account that states an annual percentage yield must also state the annual percentage yield for each tier, along with corresponding minimum balance requirements. Any dividend rates stated must appear in conjunction with the annual percentage yields for each tier.

2. *Stepped-rate accounts.* An advertisement that states a dividend rate for a stepped-rate account must state all the dividend rates and the time period that each rate is in effect.

3. *Representative examples.* An advertisement that states an annual percentage yield for a type of account (such as a term share account for a specified term) need not state the annual percentage yield applicable to every variation offered by the credit union or indicate that other maturity terms are available. In an advertisement stating that rates for an account may vary depending on the amount of the initial deposit or the term of a term share account, credit unions need not list each balance level and term offered. Instead, the advertisement may:

i. Provide a representative example of the annual percentage yields offered, clearly described as such. For example, if a credit union offers a $25 bonus on all term share accounts and the annual percentage yield will vary depending on the term selected, the credit union may provide a disclosure of the annual percentage yield as follows: "For example, our 6-month share certificate currently pays a 3.15% annual percentage yield."

ii. Indicate that various rates are available, such as by stating short-term and longer-term maturities along with the applicable annual percentage yields. "We offer share certificates with annual percentage yields that depend on the maturity you choose. For example, our one-month share certificate earns a 2.75% APY. Or, earn a 5.25% APY for a three-year share certificate."

(c) When additional disclosures are required

1. *Trigger terms.* The following are examples of information stated in advertisements that are not "trigger" terms:

i. "One, three, and five year share certificates available".

ii. "Bonus rates available".

iii. "1% over our current rate," so long as the rates are not determinable from the advertisement.

(c)(2) Time annual percentage yield is offered

1. *Specified recent date.* If an advertisement discloses an annual percentage yield as of a specified date, that date must be recent in relation to the publication or broadcast frequency of the media used. For example, the printing date of a brochure printed once for an account promotion that will be in effect for six months would be considered "recent," even though rates change during the six-month period. Dividend rates published in a daily newspaper or on television must be a rate offered shortly before (or on) the date the rates are published or broadcast. Similarly, dividend rates published in a daily newspaper or on television must be a rate reflecting either the preceding dividend period, or a prospective rate, and the option chosen should be noted.

2. *Reference to date of publication.* An advertisement may refer to the annual percentage yield as being accurate as of the date of publication, if the date is on the publication itself. For instance, an advertisement in a periodical may state that a rate is "current through the date of this issue," if the periodical shows the date.

(c)(5) Effect of fees

1. *Scope.* This requirement applies only to maintenance or activity fees as described in paragraph 8(a).

(c)(6) Features of term share accounts

(c)(6)(i) Time requirements

1. *Club accounts.* If a club account has a maturity date, but the term may vary depending on when the account is opened, credit unions may use a phrase such as: "The maturity date of this club account is November 15; its term varies depending on when the account is opened."

(c)(6)(ii) Early withdrawal penalties

1. *Discretionary penalties.* Credit unions imposing early withdrawal penalties on a case-by-case basis may disclose that they "may" (rather than "will") impose a penalty if that accurately describes the account terms.

(d) Bonuses

1. *General reference to "bonus."* General statements such as "bonus checking" or "get a bonus when you open a checking account" do not trigger the bonus disclosures.

(e) Exemption for certain advertisements

(e)(1) Certain media

(e)(1)(i)

1. *ATM messages.* Messages provided on ATM or computer screens are eligible for this exemption.

(e)(1)(iii)

1. *Tiered-rate accounts.* Solicitations for tiered-rate accounts made through telephone response machines must provide all annual percentage yields and the balance requirements applicable to each tier.

(e)(2) Indoor signs

(e)(2)(i)

1. *General.* Indoor signs include advertisements displayed on computer screens, banners, preprinted posters, and chalk or peg boards. Any advertisement inside the premises that can be retained by a member (such as a brochure or a printout from a computer) is not an indoor sign.

(e)(3) Newsletters

1. *General.* The partial exemption applies to all credit union newsletters, whether instituted before or after the compliance date of part 707. Nor must a newsletter be of any particular circulation frequency (e.g., weekly, monthly, quarterly, biannually, annually, or irregularly) or of any certain format (e.g. magazine, bulletin, broadside, circular, mimeograph, letter, or pamphlet) in order to be eligible for the partial advertising exemption.

2. *Permissible Distribution.* In order for newsletters to retain the partial advertising exemption, newsletters can be sent to existing credit union members only. Any distribution reasonably calculated to reach only members is also acceptable, such as:

i. Mailing newsletters to existing members.

ii. Distributing newsletters at a function reasonably limited to members, such as an annual meeting or member picnic.

iii. Displaying or offering newsletters at a credit union lobby, branch, or office.

3. *Impermissible Distribution.* Distributing a newsletter in a place open to nonmembers, such as a sponsor's lunch room, is not reasonably calculated to reach only members, and such newsletter would be subject to all applicable advertising rules.

§ 707.9—Enforcement and record retention.

(c) Record retention

1. *Evidence of required actions.* Credit unions comply with the regulation by demonstrating they have done the following:

i. Established and maintained procedures for paying dividends and providing timely disclosures as required by the regulation, and.

ii. Retained sample disclosures for each type account offered to members, such as account-opening disclosures, copies of advertisements, and change-in-term notices; and information regarding the dividend rates and annual percentage yields offered.

2. *Methods of retaining evidence.* Credit unions must be able to reconstruct the required disclosures or other actions. They need not keep disclosures or other business records in hard copy. Records evidencing compliance may be retained on microfilm, microfiche, or by other methods that reproduce records accurately (including computer files). Credit unions must retain copies of all printed advertisements and the text of all advertisements conveyed by electronic or broadcast media, and newsletters.

3. *Payment of dividends.* Credit unions must retain sufficient rate and balance information to permit the verification of dividends paid on an account, including the payment of dividends on the full principal balance.

Appendix A to Part 707—Annual Percentage Yield Calculation

Part I. Annual percentage yield for account disclosures and advertising purposes.

1. *Rounding for calculations.* The following are examples of permissible rounding rules for calculating dividends and the annual percentage yield:

i. The daily rate applied to a balance carried to five or more decimals. For example: .008219178%, 3.00% for a 365 day year, would be rounded to no less than .00822%.

ii. The daily dividends or interest earned carried to five or more decimals. For example; $.08219178082, daily dividends on $1,000 at 3% for a 365 day year, would be rounded to no less than $.08219.

2. *Exponents in a leap year.* The annual percentage yield formula's exponent numerator will remain 365 in leap years. The "days in term" figure used in the denominator should be consistent with the length of term used in the dividends calculation.

3. *First tier of a tiered-rate account.* When credit unions use a rate table, the first tier of a tiered rate account is to be disclosed and advertised: "Up to but not exceeding . . .", "$.01 to . . .", or similar language.

4. *Term share accounts opened in midterm.* For club accounts that meet the definition of a term share account, the annual percentage yield is based on the maximum number of days in the term not to exceed 365 days (or 366 days in a leap year).

Part II. Annual percentage yield earned for periodic statements.

1. *Balance method.* The dividend or interest figure used in the calculation of the annual percentage yield earned may be derived from the daily balance method or the average daily balance method. Regardless of the dividend calculation method, the balance used in the annual percentage yield earned formula is the average daily balance. The average daily balance calculation is the sum of the balances for each day in the period divided by the number of days in the period. The balance for each day is based on a point in time; i.e. beginning of day balance, end of day balance, closing of day balance, etc. Each day's balance, for dividend accrual and payment purposes, must be based on the same point in time and cannot be based on the day's low balance.

2. *Negative balances prohibited.* Credit unions must treat a negative account balance as zero to determine the balance on which the annual percentage yield earned is calculated. (See commentary to § 707.7(a)(2).)

A. General formula.

1. *Accrued but uncredited dividends.* To calculate the annual percentage yield earned, accrued but uncredited dividends:

i. May not be included in the balance for statements that are issued at the same time or less frequently than the account's compounding and crediting frequency. For example, if monthly statements are sent for an account that compounds dividends daily and credits dividends monthly, the balance may not be increased each day to reflect the effect of daily compounding. Assume a credit union will pay $13.70 in dividends on $100,000 for the first day, $6.85 in dividends on $50,013.70 for the second day, and $3.43 in dividends on $25,020.55 for the third day. The sum of each day's balance is $175,000 (does not include accrued, but uncredited, dividends amounts $13.70, $6.85, and $3.43), thereby resulting in an average daily balance for the three days of $58,333.33.

ii. Must be included in the balance for succeeding statements if a statement is issued more frequently than compounded dividends are credited on an account. For example, if monthly statements are sent for an account that compounds dividends daily and credits dividends quarterly, the balance for the second monthly statement would include dividends that had accrued for the prior month. Assume a credit union will pay $411.78 in dividends on 30 days of $100,000, $427.28 in dividends on 31 days of $100,411.78, and $415.23 in dividends on 30 days of $100,839.06. The balance (average daily balance in the account for the period) for the second 31 days is $100,411.78.

2. *Rounding.* The dividends earned figure used to calculate the annual percentage yield earned must be rounded to two decimals to reflect the amount actually paid. For example, if the dividends earned for a statement period is $20.074 and the credit union pays the member $20.07, the credit union must use $20.07 (not $20.074) to calculate the annual percentage yield earned. For accounts that pay dividends based on the daily balance method, compound and credit dividends or interest quarterly, and send monthly statements, the credit union may,

but need not, round accrued dividends to two decimals for calculating the "projected" or "anticipated" annual percentage yield earned on the first two monthly statements issued during the quarter. However, on the quarterly statement the dividends earned figure must reflect the amount actually paid.

3. *Compounding frequency using the average daily balance method.* Any compounding frequency, including daily compounding, can be used when calculating dividends using the average daily balance method. (See comment § 707.7(b), which does not require credit unions to compound or credit dividends at any particular frequency).

B. Special formula for use where periodic statement is sent more often than the period for which dividends are compounded.

1. *Statements triggered by Regulation E.* Credit unions may, but need not, use this formula to calculate the annual percentage yield earned for accounts that receive quarterly statements and that are subject to Regulation E's rule calling for monthly statements when an electronic fund transfer has occurred. They may do so even though no monthly statement was issued during a specific quarter. This formula must be used for accounts that compound and credit dividends quarterly and that receive monthly statements, triggered by Regulation E, which comply with the provisions of § 707.6.

2. *Days in compounding period.* Credit unions using the special annual percentage yield earned formula must use the actual number of days in the compounding period.

Appendix B to Part 707—Model Clauses and Sample Forms

1. *Modifications.* Credit unions that modify the model clauses will be deemed in compliance as long as they do not delete information required by TISA or regulation or rearrange the format so as to affect the substance or clarity of the disclosures.

2. *Format.* Credit unions may use inserts to a document (see Sample Form B–11) or fill-in blanks (see Sample Forms B–4 and B–5, which use double underlining to indicate terms that have been filled in) to show current rates, fees or other terms.3. Disclosures for opening accounts. The sample forms illustrate the information that must be provided to a member when an account is opened, as required by § 707.4(a)(1). (See § 707.4(a)(2), which states the requirements for disclosing the annual percentage yield, the dividend rate, and the maturity of a term share account in responding to a member's request.)

4. *Compliance with Regulation E.* Credit unions may satisfy certain requirements under Part 707 with disclosures that meet the requirements of Regulation E. (See § 707.3(c).) The model clauses and sample forms do not give examples of disclosures that would be covered by both this regulation and Regulation E (such as disclosing the amount of a fee for ATM usage). Credit unions should consult appendix A to Regulation E for appropriate model clauses.

5. *Duplicate disclosures.* If a requirement such as a minimum balance applies to more than one account term (to obtain a bonus and determine the annual percentage yield, for example), credit unions need not repeat the requirement for each term, as long as it is clear which terms the requirement applies to.

6. *Guide to model clauses.* In the model clauses, italicized words indicate the type of disclosure a credit union should insert in the space provided (for example, a credit union might insert "March 25, 1995" in the blank for "(date)" disclosure). Brackets and diagonals ("/") indicate a credit union must choose the alternative that describes its practice (for example, [daily balance/average daily balance]).

7. *Sample forms.* The sample forms (B–4 through B–11) serve a purpose different from the model clauses. They illustrate various ways of adapting the model clauses to specific accounts. The clauses shown relate only to the specific transactions described.

Part 708a

Conversion of Insured Credit Unions to Mutual Savings Banks

§ 708a.1 Definitions.

As used in this part:

(a) *Credit union* has the same meaning as insured credit union in section 101 of the Federal Credit Union Act.

(b) *Mutual savings bank* and *savings association* have the same meaning as in section 3 of the Federal Deposit Insurance Act.

(c) *Federal banking agencies* has the same meaning as in section 3 of the Federal Deposit Insurance Act.

(d) *Senior management official* means a chief executive officer, an assistant chief executive officer, a chief financial officer, and any other senior executive officer as defined by the appropriate federal banking agency pursuant to section 32(f) of the Federal Deposit Insurance Act, 12 U.S.C. 1831i(f).

§ 708a.2 Authority to convert.

An insured credit union, with the approval of its members, may convert to a mutual savings bank or a savings association that is in mutual form without the prior approval of the NCUA, subject to applicable law governing mutual savings banks and savings associations and the other requirements of this part.

§ 708a.3 Board of directors and membership approval.

(a) The board of directors must approve a proposal to convert by majority vote and set a date for a vote on the proposal by the members of the credit union.

(b) The membership must approve the proposal to convert by the affirmative vote of a majority of those members who vote on such proposal.

§ 708a.4 Voting procedures.

(a) A member may vote on the proposal to convert in person at a special meeting held on the date set for the vote or by written ballot filed by the member.

(b) A credit union that proposes to convert must provide written notice of its intent to convert to each member who is eligible to vote on the conversion. The notice to members must be sent by registered, certified, or regular mail with postage prepaid and postmarked 90 calendar days, 60 calendar days, and 30 calendar days before the date of the membership vote on the conversion and a ballot must be sent not less than 30 calendar days before the date of the vote.

(c) The notice to members must adequately describe the purpose and subject matter of the vote to be taken at the special meeting or by submission of the written ballot. The notice must clearly inform the member that the member may vote at the special meeting or by submitting the written ballot. The notice must state the date, time, and place of the meeting.

§ 708a.5 Notice to NCUA.

(a) The credit union must provide the Regional Director for the region where the credit union is located with notice of its intent to convert during the 90 calendar day period preceding the date of the membership vote on the conversion.

(b) The credit union must give notice to the Regional Director by providing a letter describing the material features of the conversion or a copy of the filing the credit union has made with another federal or state regulatory agency in which the credit union seeks that agency's approval of the conversion. The credit union must include with the notice to the Regional Director a copy of the notice the credit union provides to members under § 708a.4, as well as, the ballot form and all written materials the credit union has distributed or intends to distribute to the members.

(c) If it chooses, the credit union may provide the Regional Director notice of its intent to convert prior to the 90 calendar day period preceding the date of completion of the conversion. In this case, the Regional Director will make a preliminary determination regarding the methods and procedures applicable to the membership vote. The Regional Director will notify the credit union within 30 calendar days of receipt of the credit union's

notice of intent to convert if the Regional Director disapproves of the proposed methods and procedures applicable to the membership vote. The credit union's prior submission of the notice of intent does not relieve the credit union of its obligation to certify the results of the membership vote required by § 708a.6 or eliminate the right of the Regional Director to disapprove the actual methods and procedures applicable to the membership vote if the credit union fails to conduct the membership vote in a fair and legal manner.

§ 708a.6 Certification of vote on conversion proposal.

The board of directors of the converting credit union must certify the results of the membership vote to the Regional Director within 10 calendar days after the vote is taken. The board of directors must also certify at this time that the notice, ballot and other written materials provided to members were identical to those submitted pursuant to § 708a.5 or provide copies of any new or revised materials and an explanation of the reasons for the changes.

§ 708a.7 NCUA oversight of methods and procedures of membership vote.

(a) The Regional Director will issue a determination that the methods and procedures applicable to the membership vote are approved or disapproved within 10 calendar days of receipt from the credit union of the certification of the result of the membership vote required under § 708a.6.

(b) If the Regional Director disapproves of the methods by which the membership vote was taken or the procedures applicable to the membership vote, the Regional Director may direct that a new vote be taken.

(c) The Regional Director's review of the methods by which the membership vote was taken and the procedures applicable to the membership vote includes determining that the notice to members is accurate and not misleading, that all notices required by this section were timely, and that the membership vote was conducted in a fair and legal manner.

§ 708a.8 Other regulatory oversight of methods and procedures of membership vote.

The federal or state regulatory agency that will have jurisdiction over the financial institution after conversion must verify the membership vote and may direct that a new vote be taken, if it disapproves of the methods by which the membership vote was taken or the procedures applicable to the membership vote.

§ 708a.9 Completion of conversion.

(a) Upon receipt of approvals under § 708a.7 and § 708a.8 of this part, the credit union may complete the conversion transaction.

(b) Within 30 calendar days after the effective date of the conversion, the board of directors of the mutual savings bank or mutual savings association must certify completion of the transaction to the Regional Director. NCUA will cancel the insurance certificate of the credit union and, if applicable, the charter of the federal credit union.

§ 708a.10 Limit on compensation of officials.

No director or senior management official of an insured credit union may receive any economic benefit in connection with the conversion of the credit union other than compensation and other benefits paid to directors or senior management officials of the converted institution in the ordinary course of business.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Organization and Operations of Federal Credit Unions

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The Credit Union Membership Access Act modified NCUA's chartering and field of membership authority. Accordingly, NCUA is finalizing a number of amendments to its policies to update them consistent with the recent legislation.

Additionally, the final rule revises and updates NCUA's chartering and field of membership policy to reflect the advances and changes in chartering requirements since the promulgation of IRPS 94–1. The majority of the revisions reflect NCUA's policy on the types of federal credit union charters and the criteria necessary to amend a credit union's field of membership. The legislation authorizes three types of credit union charters. These charter types include a single occupational or associational common bond, a multiple common bond, or a local community, neighborhood, or rural district serving a well defined area.

Along with a comprehensive update of chartering policy, the format of the chartering manual has been changed to make it more user-friendly. The final rule further clarifies overlap issues, mergers, low-income policies regarding low income charters and service of underserved areas, the definition of immediate family member or household, and the ''once a member, always a member'' policy.

DATES: Effective date: January 1, 1999.

Applicability date: IRPS 99–1 will be applicable January 1, 1999, except for the provisions on the definition of ''local community, neighborhood or rural district, and ''immediate family member or household,'' which will be applicable March 5, 1999, unless disapproved by Congress under the major rule provisions.

ADDRESSES: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428.

FOR FURTHER INFORMATION CONTACT: J. Leonard Skiles, Chairman, Field of Membership Task Force, 4807 Spicewood Springs Road, Suite 5100, Austin, Texas 78759, or telephone (512) 231–7900; Michael J. McKenna, Senior Staff Attorney, Office of General Counsel, 1775 Duke Street, Alexandria, Virginia 22314 or telephone (703) 518–6540; Lynn K. McLaughlin, Program Officer, Office of Examination and Insurance, 1775 Duke Street, Alexandria, Virginia, or telephone (703) 518–6360.

SUPPLEMENTARY INFORMATION: In 1982, the changing negative economic environment created safety and soundness concerns that prompted the Board to revise its chartering policy to permit membership in a federal credit union to consist of multiple common bonds, provided each group possessed a common bond. Such membership could be accomplished through the chartering process, through charter amendments, or by way of merger to form a single credit union. This policy change strengthened the federal credit union system by enabling NCUA to merge credit unions that otherwise would have failed because of the loss of a sponsor or other financial or operational downturns. The policy also enabled federal credit unions to diversify their membership and become less dependent on the financial success of one sponsoring company or group. An important advantage of the policy change was that it provided access to credit union service for small groups of people who did not have the resources to charter their own credit unions. The Board issued subsequent changes to the 1982 chartering policy in 1984, 1989, 1994, 1996, and 1998, most of which addressed the multiple common bond policy.

In First National Bank and Trust Co., et al. v. *National Credit Union Administration,* 90 F.3d 525 (D.C. Cir. 1996), the U.S. Court of Appeals for the District of Columbia Circuit invalidated certain select group additions to the field of membership of a North Carolina credit union (the ''Decision''). In that case, the Court ruled that groups with unlike common bonds could not be joined to form a single credit union. Furthermore, in the consolidated cases of *First National Bank and Trust Co., et al.* v. *NCUA* and the *American Bankers Association, et al.* v. *NCUA et al.,* the U.S. District Court issued a nationwide injunction prohibiting federal credit unions from adding new select groups to their fields of membership that did not share a common bond (the ''Order''). The Decision and Order affected the operations of approximately 3,600 multiple common bond federal credit unions serving approximately 158,000 select groups.

On February 25, 1998, the U.S. Supreme Court ruled that NCUA's multiple common bond policy was impermissible under the Federal Credit Union Act (FCUA). *National Credit Union Administration* v. *First National Bank & Trust Co. et al.,* 118 S. Ct. 927 (1998). The Supreme Court affirmed the lower court's finding that groups with unlike common bonds could not be joined to form a single occupational credit union. As a result, Congress addressed the multiple common bond and other field of membership issues and recently enacted legislation reinstating NCUA's multiple common bond policy with some modifications. The Credit Union Membership Access Act (''CUMAA''), Public Law 105–219. CUMAA updated the statutory common bond rules for the first time since 1934.

Accordingly, on August 31, 1998, the Board issued a proposed rule that revised and updated NCUA's chartering and field of membership policies with a sixty day comment period. 62 FR 49164 (September 14, 1998). The policy was issued as proposed IRPS 98–3. Three hundred and sixty-nine comments were received. Comments were received from one hundred and eighty-one federal credit unions, twenty-three state chartered credit unions, thirty state credit union leagues, four national credit union trade associations, two congressmen, seventy-two banks, thirty bank trade associations, twenty credit union members, two law firms, one credit union sponsor, one certified public accountant, one consulting firm, one advocacy group and one other individual. Except for the bank and bank trade associations, most commenters were very supportive of the proposed chartering and field of membership policies, although most commenters suggested ways they would modify the final rule. Except for the section on mergers, the bank and bank trade association comments are summarized in a separate section. Although a separate section is devoted to the comments received from the bankers and bank associations, the issues they raised are addressed throughout the preamble in response to other similar comments.

The comments received were varied and addressed virtually every field of membership issue. All the comments were carefully reviewed, particularly those that expressed concern or that were in opposition to the proposed field of membership provisions, and a response to most of the issues raised is set forth in the section by section analysis of the comments. There were, however, five issues that generated numerous comments and either were confusing or proved somewhat controversial to the commenters. They were: (1) overlaps and exclusionary clauses; (2) economic advisability (the

numerical threshold for member support to charter a new credit union); (3) reasonable proximity and service facility requirements for select group additions to multiple common bond credit unions; (4) voluntary mergers of financially healthy multiple common bond credit unions; and, (5) the definition of immediate family member or household. Accordingly, these five issues are separately addressed in the preamble.

A. Overlaps and Exclusionary Clauses

Occupational and Associational Single Common Bond Credit Unions

The Board proposed that, as a general rule, NCUA will not charter two or more credit unions to serve the same single occupational or associational group. Consequently, the proposal provided overlap protection for single occupational or associational credit unions. However, the Board further proposed that an overlap would be permitted when two or more credit unions are attempting to serve the same group if the overlap's beneficial effect in meeting the convenience and needs of the members of the group proposed to be included in the field of membership clearly outweighs any adverse effect on the overlapped credit union. This language parallels the statutory requirement for multiple common bond credit unions.

The proposal set forth when NCUA would permit an overlap of an occupational or associational credit union and what NCUA considers in reviewing an overlap. The Board stated that an occupational or associational credit union will rarely, if ever, be protected from overlap by a community charter. The Board also stated that where a federally insured state credit union's field of membership is broadly stated, NCUA will exclude its field of membership from overlap protection. NCUA defines ''broadly stated'' to mean either a statewide field of membership or a field of membership that would not comport with or is inconsistent with federal field of membership policies.

Multiple Common Bond Credit Unions

The Board proposed that NCUA will generally not approve an overlap unless the expansion's beneficial effect in meeting the convenience and needs of the members of the group proposed to be included in the field of membership clearly outweighs any adverse effect on the overlapped credit union. The proposed overlap policy restated the statutory requirement for addressing overlap issues affecting multiple common bond credit unions. The proposal also set forth the issues NCUA would consider in reviewing the overlap. In general, if the overlapped credit union did not object, and NCUA determines that there are no safety and soundness problems, the overlap would be permitted. If, however, the overlapped credit union objected to the overlap, a more detailed overlap analysis would be required.

The Board proposed that overlaps between multiple common bond credit unions and community chartered credit unions would be permitted without performing an overlap analysis, since NCUA has determined that, in these types of overlaps, the benefit of the overlap to the member will always outweigh the harm to either credit union. The Board stated that a multiple common bond credit union would rarely, if ever, be protected from overlap by a community charter.

Community Charters

The Board proposed that a credit union seeking a community charter contact all federally insured credit unions with a service facility in the proposed service area. Notwithstanding the requirement to contact all credit unions within the proposed service area, the proposal permitted a community credit union to overlap any other type of credit union charter. The Board stated that a community charter would rarely, if ever, be protected from overlap by a single occupational, single associational or multiple common bond credit union. If safety and soundness concerns existed, the Board proposed providing overlap protection from a community charter for a limited period of time, generally 12 to 24 months.

In the past, exclusionary clauses were permitted for reasons other than for safety and soundness, such as when there was an agreement between the overlapping credit unions. An exclusionary clause, under circumstances other than for safety and soundness, would not be permitted under the proposal if the overlapping credit union was a community charter. The Board requested specific comment as to whether exclusionary clauses are appropriate for community charters and, if so, under what circumstances.

Comments

There were numerous comments on overlaps and how NCUA should address this issue. For example, seventeen commenters objected to overlap protection for any credit union regardless of the reason. Eleven commenters objected to overlap protection, except if the overlap causes significant harm to the existence of another credit union. Five commenters approved of NCUA's proposed policy on overlaps. One commenter stated that overlap procedures should be the same for all types of credit unions. Five commenters recommended overlap protection for small credit unions. One commenter recommended that NCUA carefully review any overlaps of small credit unions. Two commenters recommended overlap protection. Many other commenters suggested different methods of addressing overlap issues.

There were also numerous comments on exclusionary clauses. For example, forty-two commenters suggested that NCUA provide a procedure to allow one credit union to petition to remove existing exclusionary clauses, regardless of charter type. A number of these commenters suggested that exclusionary clauses are almost impossible to police and frustrate the consumer. One commenter stated that NCUA should rarely impose exclusionary clauses. Seven commenters believed the removal of an exclusionary clause should be approved only if both credit unions agreed. Three commenters opposed a process to remove exclusionary clauses. Many other commenters addressed the use of exclusionary clauses.

Three commenters approved of the overlap rules for community charters. Three commenters stated that exclusionary clauses should never be a part of a community charter's field of membership. One commenter stated that exclusionary clauses should rarely be used. Five commenters requested overlap protection from community credit unions. Three commenters requested overlap protection for community credit unions. Three commenters recommended exclusionary clauses for small credit unions that are overlapped by community charters. Three commenters stated that only one credit union should be chartered per community.

Forty-two commenters supported the proposal to provide a process for removing existing exclusionary clauses from community charters. Many of these commenters did not believe that two credit unions should be required to agree to remove the exclusionary clause. Seven commenters believed that an exclusionary clause should be removed only if the two affected credit unions agreed. A number of these commenters suggested that exclusionary clauses are almost impossible to police and frustrate the consumer. Three commenters opposed a process to remove exclusionary clauses.

NCUA Board Analysis and Decision on Overlaps and Exclusionary Clauses

In formulating its opinion on overlaps, NCUA considered not only the comments in response to the current proposal, but also the information gathered in the internal review of the overlap policies permitted under IRPS 94–1 and previous field of membership policies. In the internal review of 58 overlapped credit unions, no long-term adverse financial trends were discovered. The information tended to support the contention that overlaps have not caused any credit union to fail, even though there was, in a limited number of cases, a temporary loss in market share. This finding was consistent with other studies on overlaps, including a recent analysis by the Office of Examination and Insurance on 14 overlapped credit unions where the original recommendation to include an exclusionary clause was not approved by the Board. Overall, the overlapped credit unions did not suffer any harm and reported positive financial trends. Most credit unions experienced an increase in shares, assets, and loans. Delinquency declined and share and loan growth improved. The earlier research was supplemented by a random survey of federally insured credit unions that obtained a response rate of 57 percent. Of the 642 responding credit unions, 284 were overlapped and 34 overlapped other credit unions. In summary, 52 percent of the responding credit unions viewed field of membership overlaps as harmful for credit unions while 48 percent reported overlaps were beneficial. Interestingly, however, when viewed as harmful or beneficial for the credit union members, the opinions were decidedly different. In response to this issue, 82 percent indicated that overlaps benefit members.

The proposed policy on overlaps took into consideration NCUA's experience, the internal review and the survey. The final rule also considered the commenters' opinions. The Board's opinion remains that the overlap policy, as enunciated in the proposal for single occupational and associational credit unions, is supportable and in the best interests of credit unions. In general, credit unions will not be chartered to serve the same common bond group, but incidental overlaps, as defined below, would be permitted. The final rule includes a provision that allows a credit union that has an existing exclusionary clause to petition NCUA to have the exclusionary clause removed.

A decision on whether the clause will be removed will be based on an analysis of the impact of removing the clause on the overlapped credit union.

This same concept adopted for single common bond credit unions also applies to multiple common bond credit unions in that an overlap analysis, except for incidental overlaps, will be required before a group will be added to a credit union's field of membership. This is a statutory requirement. An overlap will not be permitted unless the expansion's beneficial effect in meeting the convenience and needs of the members of the group proposed to be included in the field of membership clearly outweighs any adverse effect on the overlapped credit union. The final rule includes the same criteria set forth in the proposed rule relative to what the regional director will consider in determining whether an overlap will be permitted.

The final rule, however, clarifies that an overlap analysis will not be required if the group to be added has 200 primary potential members or less. In view of the fact that approximately one-third of the primary potential members join a credit union, the Board believes a group of 200 primary potential members or less will be considered incidental. That is, the benefit to the members will always outweigh the harm to the credit union. Accordingly, a credit union applying to add a group of 200 or less primary potential members will only have to complete the 4015-EZ, which is a shortened version of the standard 4015 (the application for a field of membership amendment). No overlap analysis is required if the group being added is 200 or less.

The overlap policy for community credit unions recognizes the operational difficulty in enforcing exclusionary clauses. Additionally, it recognizes that credit union members will benefit if additional credit union choices are made available. Accordingly, it is the Board's view that community credit unions should be allowed to overlap, with a minor exception for newly chartered single common bond or multiple common bond credit unions, any credit union within the community. Consequently, no overlap analysis will be required for any credit union within a proposed community credit union's well defined area unless it is a newly chartered credit union (chartered less than 2 years). Although the commenters requested a longer time frame for protection from a newly chartered community charter (by way of conversion or a new credit union charter), the Board is only providing protection through the inclusion of an exclusionary clause for a period of 12 to 24 months from the date of the overlapped credit union's charter for a new single common bond or multiple common bond credit union. If safety and soundness concerns exist, the regional director may extend the exclusionary clause protection for a period that does not exceed 60 months from the date the overlapped credit union was chartered. Unlike the proposed rule, no overlap protection will be provided any community charter.

B. Economic Advisability

NCUA's proposed provisions on new charters and charter expansions emphasized that NCUA will evaluate the economic advisability of the proposed institution or expansion as well as its effect on other credit unions. While NCUA did not set a minimum field of membership size for chartering a federal credit union, the Board suggested, based on historical data and evidence of economic viability, that a credit union with fewer than 3,000 primary potential members (e.g., employees of a corporation or members of an association) may not be economically advisable. Therefore, a charter applicant with a proposed field of membership of fewer than 3,000 primary potential members may have to provide more support than a proposed credit union with a larger field of membership in order to demonstrate that it is economically advisable and that it will have a reasonable chance to succeed. The 3,000 primary potential member threshold number is also operationally consistent with the multiple common bond expansion requirements. The Board specifically requested comments on whether the economic advisability number should be set at a lower or higher level.

Comments

Fifty-one commenters supported the 3,000 primary potential member number as a useful threshold for defining the viability of a new credit union. A few commenters stated that the 3,000 minimum presumption promotes consistency with the statutorily required 3,000 member cap for the addition of a new select group in a multiple common bond credit union. A number of these commenters stated that NCUA should be flexible in determining how many people are necessary to start a new credit union. These commenters suggested that NCUA consider other factors in determining viability such as the ability to obtain adequate capitalization and the level of resources. Fourteen commenters believed the economic advisability number is low and six suggested a number in excess of

5,000 primary potential members as a threshold for viability. A few commenters stated that the 3,000 threshold is almost meaningless in today's economy. These commenters stated that consumers are not going to wait for a credit union to grow to offer financial services.

Twenty-one commenters did not agree with the economic advisability number. Ten commenters believed the economic advisability number is too high. A number of these commenters stated that NCUA should be flexible with any numerical member threshold. A number of commenters further stated that, if a smaller group is financially sound, NCUA should charter the credit union. Conversely, if a larger group is not financially sound, then NCUA should not charter the credit union. One commenter believed the 3,000 threshold may soon become a requirement which will be particularly onerous to the chartering of faith-based credit unions. Some commenters requested that NCUA provide the rationale for choosing the 3,000 number threshold.

NCUA Board Analysis and Decision on Economic Advisability

The Board is adopting the 3,000 primary potential member threshold in the final rule. This position is consistent with congressional intent as well as NCUA experience. This threshold is not intended to undermine the statutory requirement to encourage the formation of new credit unions. Rather, it has been established to provide potential new charters necessary advice and guidance to charter a successful credit union. Any group desiring to form its own credit union will be given every opportunity to demonstrate it has met the economic advisability requirements. Additionally, any group not desiring to charter its own credit union will be reviewed to determine if in fact it can be separately chartered.

IRPS 94–1 established the economic advisability threshold as 500 primary potential members. Notwithstanding this threshold number of 500, the Board's opinion has long been that the 500 primary potential members threshold was extremely low, particularly in view of the fact that only approximately one-third of the primary potential members join. Accordingly, there have been numerous recommendations that the 500 threshold number should be increased.

Since 1996, NCUA has chartered 29 new credit unions. Only one of these new charters had a primary potential membership that was less than 3,000. While there are many factors impacting why the number of new charters since 1996 is low, experience has indicated that one critical factor is the financial service expectation of the potential members. That is, what type of financial service will the new credit union provide? If the financial service is limited, then it will not meet the members' financial service expectations and, as a result, the credit union will not be fully supported. The analysis of whether a new group can form a new credit union must take the members reasonable expectations into consideration. Failure to do so would put the National Credit Union Share Insurance Fund (''NCUSIF'') at risk.

The Board's view is that the 3,000 primary potential membership threshold is an economically advisable number for potential new charters, but not an absolute requirement. This distinction is important. For example, there are approximately 3,100 federal credit unions with primary potential members of less than 3,000. Approximately 700 of those have primary potential members of 500 or less. For the most part, however, at the time of their charter, economic conditions and the financial service expectations of the credit union members were different. These differences provided the credit unions an opportunity to become established and develop a loyalty base under marketplace expectations that significantly differ from those of today. The Board must consider the evolving nature of the financial marketplace. It would be remiss simply to say that, since a lower threshold number worked in the past, there is no need to change the economic advisability number requirement today.

The Board's intent is that every group being added to a multiple common bond credit union should be analyzed to determine whether it has the capability and desire to support an independent operation. Indeed, that is the intent of the legislation. This requirement, however, must be balanced with operational feasibility. To overlook the complexities of providing financial services will only lead to additional supervisory problems. The regulatory approach, therefore, should incorporate known economic factors and the likelihood of success in establishing and managing a new credit union in today's marketplace. To this end, the Board's intent is that a group desiring a separate charter should have every reasonable opportunity to form a new credit union. As stated earlier, the 3,000 primary potential member threshold is not an absolute, but simply a threshold. There are numerous examples where smaller groups can and should have a separate credit union. For example, faith based credit unions, as one commenter suggested, may be uniquely positioned to be separately chartered.

The expectation is that those groups above the threshold of 3,000 primary potential members must be able to demonstrate why they cannot satisfactorily form a separate credit union if they want to be added to another credit union. Statutorily, there is a presumption that, unless certain exceptions apply, a group larger than 3,000 should form its own credit union. That is, the exception criteria will be closely evaluated. Groups below the 3,000 threshold, however, must be able to demonstrate why they can successfully operate a credit union. In other words, the emphasis shifts based on the size of the group. For example, a group of 525 may have more difficulty demonstrating economic advisability than a group of 3,000. This is a balanced approach to the financial service expectations of the members, the intent of Congress that all groups should be analyzed to determine if the formation of a separately chartered credit union is practicable and consistent with economic advisability criteria, and those factors that are historically important in evaluating a new charter applicant from a regulatory standpoint. This is an economically and operationally sound approach to chartering new credit unions. The Board believes it must not only encourage new charters, but also ensure to the fullest extent possible that those groups receiving a separate charter will have a reasonable basis for success and thereby avoid unnecessary risks to the NCUSIF. Accordingly, the field of membership rules on economic advisability must reflect known economic factors and the potential risks to the NCUSIF. It is essential, therefore, that the approval process incorporate the necessary regulatory analysis to make these determinations.

The question was raised concerning the standard that will be used in determining what level of services is adequate in determining the separate charter analysis vis-á-vis an already established credit union. That is, if a new charter can only offer limited services, but an existing charter offers a full service menu, will that fact in of itself be sufficient to determine that a separate charter is not required. One commenter stated that ''the economic advisability does not take into consideration whether the group would be able to have similar services.'' The Board's opinion is that such a standard would circumvent the intent of the statute and, if adopted, the potential for new charters would be drastically

reduced. Except in very rare circumstances, no new credit union charter can offer the same financial services of an established credit union. Accordingly, a similar service criterion cannot be a factor in determining whether a new group will meet that standard. However, if the group is already in the field of membership of a credit union and has been receiving expanded financial services, it is reasonable to consider that factor. This may occur in voluntary merger situations. For that reason, out of fairness to such a group, the failure to provide similar or equal services is more important, but not necessarily dispositive of the issue.

It is also incumbent on the Board to establish rules that are not unnecessarily burdensome. For that reason, it has adopted the presumptive factor of 3,000 in determining what criteria will be applicable. In adopting the 3,000 primary potential member threshold factor, the Board recognizes that newly chartered credit unions in today's financial marketplace have unique challenges. Those groups that can or should be able to meet those challenges, regardless of size, will be required to form a separate credit union unless they meet the common bond requirements. As the legislation directs, the Board will encourage the formation of separately chartered credit unions if it is prudent and economically advisable. Important factors in making this determination, however, are the desire and intent of the group and the sponsor support. In other words, to ignore the group's administrative capability may lead to unnecessary supervisory problems in the future. While the intent of the group and sponsor support cannot be ignored and will carry great weight, they are not the sole factors. The final decision must be based on an independent regulatory analysis in consideration of the remaining factors specified in the regulation.

Four commenters recommended that NCUA include in its definition of economic advisability the statutory language from CUMAA that encourages the formation of separately chartered credit unions ''whenever practicable and consistent with reasonable standards for the safe and sound operation of the credit union.'' 12 U.S.C. 1759(f)(1)(A). The Board agrees with these commenters and has incorporated this change into the final rule in the discussion on multiple common bond charter expansions.

C. Reasonable Proximity and Service Facility Requirements for Select Group Additions

CUMAA reinstated NCUA's multiple common bond policy, as set forth in IRPS 94–1, with significant modifications. A multiple common bond credit union may serve a combination of distinct, definable, occupational and/or associational common bonds. Multiple common bond credit unions can add groups with dissimilar common bonds, which are called select groups. These groups must be within reasonable proximity of the credit union. That is, the groups must be within the service area of one of the credit union's service facilities.

Comments

Twenty-five commenters agreed with NCUA's definition of reasonable proximity, although a number of these commenters stated NCUA should give consideration to accessibility via the internet and home banking.

Six commenters were unsure as to what is meant by ''within the service area'' and questioned how that term will be applied. Ten commenters stated that the reasonable proximity standard should not be applied in a blanket fashion. For example, some of these commenters stated that the distance should be farther in rural areas for the purpose of determining what constitutes reasonable proximity.

Fifty-two commenters disagreed with NCUA's definition of reasonable proximity. Most of these commenters believed it is not necessary, legally or for safety and soundness reasons, since credit unions can automatically and electronically deliver services around the globe. Some commenters stated that NCUA's definition of reasonable proximity goes well beyond congressional intent. These commenters stated that Congress intended that groups be located within a close geographic area to the credit union.

The Board defined a service facility as a place where shares are accepted for members' accounts, loan applications are accepted, and loans are disbursed. This definition included a credit union owned branch, a shared branch, or a credit union owned electronic facility that meets, at a minimum, these requirements. This definition did not include an ATM. Thirty-one commenters agreed with NCUA's definition of service facility. One commenter requested that NCUA specifically state that a mobile branch is a service facility for multiple common bond expansions.

Thirty-one commenters did not approve of NCUA's definition of service facility. Most of these commenters believed that, with the advent of electronic services, a ''brick and mortar'' facility is obsolete. Nineteen commenters requested that ATMs be included as a service facility. Some of these commenters recommended deleting parts of the definition that requires the facility to be a place where deposits are made, loan applications are accepted and funds disbursed. A few commenters stated that NCUA's definition of service facility goes well beyond congressional intent.

NCUA Board Analysis and Decision on Reasonable Proximity

As indicated above, there were numerous comments on the proposed definition of ''reasonable proximity.'' Suggestions ranged from mileage to electronic limitations. Reasonable proximity is an essential factor in determining whether a group can be added to a multiple common bond credit union. The Board's view is that CUMAA and its legislative history sets forth the requirement that reasonable proximity should be a geographic limitation. That is, the group to be added must be within reasonable proximity geographically to the credit union. Therefore, the advantages acquired from advancing technologies do not undermine what the Board considers is the congressionally mandated requirement that the group to be added must be within ''reasonable proximity'' to the credit union.

However, it is not the Board's view that the location of the group must be within reasonable proximity to the main credit union office only. This would be an overly restrictive requirement. Since reasonable proximity is not specifically defined in the legislation, the terms service area and service facility were proposed in an effort to establish the limits of a geographic reasonable proximity. That is, the group to be added must be within the service area of a service facility of the credit union. As specified in the final rule, service facility does not include an ATM. The legislative history of CUMAA is clear that NCUA should not treat ATMs as service facilities for select group expansions. Therefore, the final rule excludes an ATM as a service facility. A service facility will include, however, a credit union owned branch, a shared branch, a mobile branch that goes to the same location on a weekly basis, or a credit union owned electronic facility. Additionally, the Board's view is that an office that is open on a regularly scheduled weekly basis will also qualify as a service facility. This will enhance the development of credit union

services in low income and underserved areas. At a minimum, to qualify as a service facility, the member must be able to deposit funds, apply for a loan, and obtain funds on approved loans.

Past experience with mileage limitations indicates that using distance factors to define reasonable proximity would create numerous inequities. Rural areas obviously differ from urban areas. Small towns differ from large cities. The vast geographic territory combined with the sparse population in the southwest and western mountain areas differ from the rural areas of the east. While mileage limitations often facilitate regulatory decisions, frequently, they are artificial and cause unfair results simply because of small geographic differences. Accordingly, mileage limitations were deemed inappropriate and not advisable. Essentially, the service area means that a member can reasonably access the service facility. In rural areas this may include distances encompassing several counties. In a densely populated area, it may be a portion of a city.

D. Voluntary Mergers of Financially Healthy Multiple Common Bond Credit Unions

The proposal set forth the requirements for the merger into, and by, a multiple common bond credit union. In making the proposal, the Board was mindful of the historic importance of mergers to the financial stability of credit unions and of the importance of credit unions to independently determine what is in the best interests of their members. Often in today's marketplace, membership diversity and growth are essential ingredients to financially strong credit unions. Merging credit unions is crucial to the entire credit union system and helps reduce the risk to the NCUSIF. Generally, credit union officials are best suited to judge when a healthy credit union's membership and financial strength will be enhanced by a merger. In making its proposal, the Board sought to balance these realities against its responsibility to assure mergers are consistent with the statutory requirements of CUMAA and that they do not weaken credit unions or increase the risk to the NCUSIF.

The Board proposed, that generally, the requirements applicable to field of membership expansions apply to a credit union merging into a multiple common bond credit union. That is, if the continuing credit union in a proposed merger is federally chartered and the merging credit union has a select group of 3,000 or more persons (excluding family members), the merger can be approved only if NCUA's expansion requirements are met. If the expansion requirements are not met, this would require a credit union to spin-off a select group of 3,000 or more persons from the merging credit union or the merger could not be approved. In all cases, the individual groups in the merging credit union would have to meet the multiple common bond policies.

Comments

Only one commenter supported the proposed merger process. Sixty-two commenters believed financially healthy multiple common bond credit unions should be permitted to merge without the constraints of the proposed 3,000 limitation approval process. Twenty-two of these commenters stated that CUMAA did not change NCUA's existing merger authority under Section 205(b) of the Federal Credit Union Act (''FCUA'') and that the 3,000 numerical limitations only applies to field of membership expansions and not mergers. Generally, all bank and bank trade organizations opposed the proposal. They argued that CUMAA and its legislative history require that the statutory standards, including the 3,000 numerical limitation, apply whether a single group is being added to a credit union or whether a voluntary merger of a credit union with many groups is being contemplated.

NCUA Board Analysis and Decision on Voluntary Mergers of Multiple Common Bond Credit Unions

In response to the comments raised by credit union trade organizations and bank trade organizations, as well as a further review of the statutory language and legislative history, the Board has decided to amend its proposal. Recognizing the importance of mergers to a stable healthy credit union system, the final rule permits the voluntary merger of healthy multiple common bond credit unions containing select employee groups of less than 3,000 primary potential members without regard to the statutory analysis that is required when non-affiliated groups of less than 3,000 members seek to join an existing credit union. In credit unions seeking to merge containing groups with 3,000 or more members, the provisions of Section 101(d)(2)(A) of CUMAA must be met or the groups in excess of 3,000 will have to be spun off in order for the merger to proceed. All credit unions seeking a voluntary merger will still be required to comply with the requirements of Section 205(b) of the FCUA, 12 U.S.C. 205(b). However, because of statutory requirements, a financially healthy single common bond credit union with a primary potential membership in excess of 3,000 primary potential members cannot merge into a multiple common bond credit union, absent supervisory reasons.

In making this change the Board is mindful of its obligation to be faithful to the statutory language. In doing so, ''the starting point must be the language of the statute itself.'' *Int'l Brotherhood of Electrical Workers* v. *NLRB*, 814 F.2d 697, 710 (D.C. Cir. 1987) (quoting *Lewis* v. *United States*, 445 U.S. 55, 60 (1980). Frequently, the ''best guide to what a statute means is what it says.'' *Stewart* v. *National Shopmen Pension Fund*, 730 F.2d 1552, 1561 (D.C. Cir.) *cert. denied* 469 U.S. 834 (1984) (emphasis in original). Section 101(b)(2) of CUMAA authorizes multiple common bond credit unions. Section 101(d)(1) provides that groups of fewer than 3,000 members can generally be added to a multiple common bond credit union provided certain criteria are met. Section 102 sets forth the statutory criteria that must be met. Taken together, these provisions address the chartering of new multiple common bond credit unions and the addition of non-affiliated groups of less than 3,000 members to existing institutions. Though Congress could have done so, it did not include any language discussing or limiting NCUA's ability to authorize the merger of existing multiple common bond credit unions containing groups with less than 3,000 members.

A merger involves the combination of pre-existing corporations, a process different both legally and practically from the addition of a group to a credit union. Mergers of multiple common bond credit unions after adoption of this rule will involve groups already added to the merging credit unions, either after consideration of the criteria set forth in Section 102 of CUMAA, or through the grandfather provision in Section 101(c). In either case, they would already be contained within the field of membership of an existing multiple common bond credit union. Had Congress expected each such group to be evaluated again in accordance with the criteria set forth in Section 102, it could easily have said so.

Congress next provided two exceptions to the 3,000 member limitation in Sections 101(d)(2)(A) and (B) of CUMAA. The first allows the addition of groups of 3,000 or more members if the Board finds that such a group could not reasonably establish its own credit union because: (1) the group lacks sufficient support to form a credit union; (2) it is unlikely to be successful in establishing and managing a credit

union; and (3) the group would be unlikely to operate a safe and sound credit union.

The next exception contains the first mention of mergers in the statute. Section 101(d)(2)(B) expressly eliminates any restriction on the addition of groups of 3,000 or more if the group is being transferred as part of a merger for safety and soundness reasons. By implication, it is the Board's view that, if there are no safety and soundness concerns, groups of 3,000 or more cannot be included as part of a merger unless the statutory criteria of Section 101(d)(2)(A) are met. The Report of the Committee on Banking and Financial Services supports this conclusion. In discussing the exceptions provided in Section 101(d)(2), the report states ''the Board may merge or consolidate a group with over 3,000 members with another credit union for supervisory reasons. The Committee does not intend for these exceptions to provide broad discretion to the Board to permit larger groups to be incorporated within or merged with other credit unions. The exceptions are intended to apply where the Board has sufficient evidence to support a finding that creation of a separately chartered credit union, or the continued operation of an existing credit union, present safety and soundness concerns.'' H.R. Rep. No. 105–472, 105th Cong., 2nd Sess. 19 (1998). Notably absent from this discussion is any mention of limitations on mergers of credit unions containing groups of less than 3,000 members.

In Section 101(d)(2)(C), Congress created an exception applicable to a limited number of cases where a merger was in process, but not completed, under the NCUA's previous field of membership policy. That policy was enjoined in the litigation that led to the passage of CUMAA. The Board believes this provision was intended as a one time authorization to complete a limited number of in process mergers without regard to the size of the groups in the institutions involved.

Finally, the Board does not believe that Congress' failure to amend Section 205(b)(2)–(3) of the FCUA supports a conclusion that Congress intended no limitation on voluntary mergers of credit unions. Section 205(b) does not provide independent statutory authority to allow mergers, but rather permits the Board to regulate voluntary mergers that are otherwise authorized by law. In contrast, Section 205(h) allows the Board to authorize mergers in emergency situations ''[n]otwithstanding any other provision of law.'' Thus, the Board may regulate and approve mergers under 205(b) only if they do not conflict with the limited restrictions, discussed above, provided by CUMAA's amendments to the FCUA.

The limitation on voluntary mergers applicable to multiple common bond credit unions does not apply to the mergers of single common bond credit unions or community charter mergers. The Board recognizes that the numerical limitation in the voluntary merger rule for multiple common bond charters may, in rare circumstances, encourage a federal credit union to seek a state charter credit union as a merger partner if the state rules are more permissive.

The proposal also clarified requirements for mergers of multiple common bond credit unions for safety and soundness reasons and emergency situations. The numerical limitation would not apply to mergers where there are safety and soundness concerns or the emergency criteria exist. Four commenters requested that NCUA expand the discussion on supervisory mergers. Two commenters recommended that NCUA state that the numerical limitation does not apply for safety and soundness mergers even if the credit union is not insolvent or in danger of insolvency. One commenter stated that, when merging two credit unions for supervisory reasons, nonmember employees of the merging credit union would still be eligible for membership in the continuing credit union. The Board has expanded the discussion on mergers for safety and soundness reasons and has specifically stated that the credit union need not be insolvent or in danger of insolvency for NCUA to use this statutory authority. In a supervisory merger, the continuing credit union is able to serve all of the groups from the discontinuing credit union and not just members of record.

Twelve commenters stated that supervisory mergers and emergency mergers should require all credit unions in the area of the merging credit union to be notified so that they have an opportunity to be considered as a merger partner. One commenter stated that when NCUA is seeking out merger partners for a credit union, it should give credit unions in the same state the right of first refusal. NCUA will attempt to find local merger partners for a credit union that is involved in supervisory or emergency mergers. However, the Board is not requiring notification of all local credit unions. The Board believes such a requirement would be a needless bureaucratic hurdle and cause unnecessary delay. The delay could exacerbate existing problems for the soon to be merged credit union. The Board believes that in such cases it could create losses for the NCUSIF, as well as the credit union that accepts the troubled credit union as a merger partner. However, the Board is reemphasizing that it will expect the regions to look first to local merger partners before considering other credit unions. If the Board is notified that the regions are not conducting the process in this way, the Board may consider a more formalized process.

E. Immediate Family Member or Household

As mandated by CUMAA, the Board is required to define ''immediate family member or household.'' The definition of these terms is designated as a major rule and must be submitted to Congress for approval. Accordingly, the Board proposed to define ''members of their immediate families'' as related persons i.e., blood, marriage, or other recognized family relationships in the same household (under the same roof), or if not in the same household, as a grandparent, parent, spouse, sibling, child, or grandchild. For the purposes of this definition, immediate family member included stepparents, stepchildren, and stepsiblings, and, although not specifically stated, adopted children or any other legally recognized family relationship. The Board also stated that the immediate family member must be related to the credit union member. In other words, once a person becomes a member, then that person's immediate family could join. The proposed definition was controversial and generated numerous comments.

Comments

Thirty-seven commenters generally approved of NCUA's definition of ''immediate family member.'' Seven commenters further stated that it will have a positive effect on a credit union's ability to grow. Five commenters believed NCUA's proposed definition of ''immediate family member'' would have a neutral effect on their credit unions.

One hundred and seven commenters generally disagreed with NCUA's definition of ''immediate family member'' and twenty-three of these commenters further stated that it would have a negative effect on a credit union's ability to grow. Twenty-seven of these commenters stated that a credit union should be able to define ''immediate family members.'' Twenty-six commenters requested that in-laws, aunts, uncles and cousins outside the household be included in the definition of ''immediate family member.'' Fifteen commenters suggested that NCUA define ''immediate family member'' to

include all relatives by blood or marriage. Five commenters suggested that NCUA should limit the definition of ''immediate family member'' to those persons directly related by blood, marriage, or other recognized family relationship. Two commenters requested that any existing immediate family member definition as described in the existing charter of a credit union be grandfathered.

Twenty-four commenters questioned whether adopted children were part of the ''immediate family member'' definition and requested they be included within the definition. Two commenters requested that NCUA specifically state that custodial and guardianship arrangements are encompassed by the ''immediate family'' definition.

Nine commenters requested one definition for immediate family member and one definition for household member. These commenters believed that persons living under the same roof, even if not in the same immediate family, are still eligible for membership. Twenty-one commenters requested domestic partners and other nontraditional family relationships be included in the definition of ''immediate family member.'' Thirty-two commenters asked for clarification on the definition of what is a recognized family relationship. One commenter specifically did not want clarification. A number of commenters requested that the final rule clarify what sources, such as state laws or regulations credit union may use as a reference to determine other family recognized relationships, as well as who does the recognizing—the credit union, the credit union's sponsor, or the state where the credit union is located.

Forty-nine commenters stated that the immediate family member should be able to join, even if the primary member has not joined. Most of these commenters stated that this interpretation is permitted by CUMAA. Thirty-nine commenters requested that credit unions have the ability to adopt a more restrictive definition. Three commenters requested that NCUA provide guidance as to what procedures, if any, credit unions need to follow to conform to the new immediate family member definition.

NCUA Board Analysis and Decision on Immediate Family Member or Household

In initially addressing the issue of immediate family member or household, the Board combined the eligibility requirements for the immediate family and household members into one inclusive definition based on traditional relationships of blood, marriage or other recognized family relationship. Within a household, any person related by blood, marriage or other recognized family relationship would qualify. Outside the household, which included those family relationships not living in the same residence, the Board proposed that the immediate family member relationship would be limited to a spouse, child, sibling, parent, grandparent or grandchild.

The initial proposed definition was narrowly construed by the Board. The Board considered the fact that the statute specifically states that ''[n]o individual shall be eligible for membership in a credit union on the basis of the relationship of the individual to another person who is eligible for membership in the credit union'' unless the individual is ''a member of the immediate family or household.'' For that reason, the Board required that, except for the immediate family member of the primary member, the ability of an immediate family member to join be based on that person's immediate family member having joined, as opposed to simply being eligible to join. In other words, before an immediate family member of a member's child could join, the child would first have to join the credit union.

In proposing the definition of immediate family member, the Board took notice of the fact that Congress intended some limitation of the definition of family member since it defined that term with the qualifier ''immediate.'' Accordingly, an open-ended definition of family member would not be consistent with the statutory language and, therefore, was deemed inappropriate. A definition that included any family member related by blood or marriage was considered unduly expansive. Consequently, the proposed definition followed a more narrow meaning of immediate family member as applied to fields of membership and the common bond concept.

Many commenters, however, took strong issue with the Board's proposed definition and approach to defining immediate family member. In consideration of those comments, the Board is adopting a modified definition which, while being more expansive than the proposed definition, retains the essential requirement that the definition cannot be defined by the credit union. After again reviewing the statutory language, the Board has determined that membership eligibility based on family relationships or household should be segregated and defined separately. The proposed definition of ''immediate family member'' is retained. That is, immediate family member eligibility is limited to a spouse, child, sibling, parent, grandparent or grandchild if not living in the same residence. Stepchildren, stepparents, stepsiblings and adopted children, as previously proposed and intended, are included in this definition. Once an immediate family member joins, then that person's immediate family would be eligible to join.

Household is defined as persons living in the same residence and who maintain a single economic unit. Included in this definition is any person who is a permanent member of and participates in the maintenance of the household. For example, two people sharing an apartment would be considered a household. In turn, the immediate family member of each member of the household who joins could also join because eligibility is then tied to the member. However, a fraternity, sorority, or condominium complex would not be considered a single economic unit. Individual residences in a condominium or apartment complex would qualify as a single economic unit. The definition of household contemplates or intends some permanency and not simply someone who is visiting for a short period. Domestic partners would be included in the household definition, since they share a residence and qualify as a single economic unit, as would anyone who lives in the household and demonstrate a degree of permanency. Legal guardian relationships are considered part of the household definition.

CUMAA does not permit NCUA to grandfather existing definitions or allow credit unions to define ''immediate family or household.'' CUMAA requires NCUA to define ''immediate family or household and although a credit union can adopt a more restrictive definition than NCUA's, it cannot establish a more expansive definition. The flexibility to adopt a more restrictive definition results from potential operational concerns. For example, a sponsor may restrict accessibility to the credit union office located on the sponsor's property.

Unless a federal credit union adopts a more restrictive definition of an ''immediate family or household'' through a board policy, NCUA's definition will automatically apply. That is, absent a board of directors' policy stating otherwise, a credit union may use NCUA's definition without taking any other action. However, a credit union should update its bylaws to

delete its prior definition of immediate family member. The Board believes that its definition of ''immediate family member or household'' is reasonable, and judging from the commenters, more restrictive than the definition used by many credit unions.

The proposal did not explicitly address whether the primary member must first join the credit union before the immediate family member can join. NCUA's intent was that the primary member need not join before the immediate member joins. Thus, the final rule sets forth NCUA's long-standing policy that the immediate family or household member may join the credit union even if the eligible primary member has not joined. However, once the primary member leaves the field of membership, the individual's immediate family or household members are no longer eligible to join through that person.

F. Section-by-Section Analysis

I. Chapter 1 of the Chartering Manual

Chapter 1 set forth the goals of NCUA's chartering policy and the requirements and procedures for chartering a new federal credit union. One commenter stated that NCUA should have an additional goal ''to support the continuing success of existing credit unions.'' The Board is not specifically stating this as a chartering goal since it is already part of NCUA's continuing regulatory mission. One commenter recommended that NCUA state an additional goal to preserve and foster the cooperative nature of credit unions. Likewise, the Board does not need to explicitly state this goal since it is inherently part of the credit union system.

Chapter 1 encouraged the formation of newly chartered federal credit unions and the use of mentor relationships with existing, well-managed credit unions. The Board stated that experienced credit unions are a valuable resource to newly chartered credit unions and can provide needed guidance and assistance. Forty-one commenters expressed support for credit unions mentoring new credit unions. One commenter opposed mentoring relationships. Three commenters stated that NCUA should state that mentoring is not required. Three commenters stated that NCUA should provide incentives for credit unions to engage in mentoring relationships. The Board, in the final regulation, continues to encourage mentoring relationships. However, mentoring is not a regulatory requirement. The main incentive for mentoring is the cooperative nature of credit unions and the social benefit of a healthy credit union system.

On the issue of name selection, the proposal stated that the word ''community'' can only be included in the name of federal credit unions that have been granted a community charter. One commenter opposed this limitation. The Board has revisited this issue and will grandfather existing non-community charters with the word ''community'' in their names. However, to avoid confusion, NCUA will not grant a new charter or a name change with the word ''community'' in the name, unless the credit union is a community charter.

Chapter 1 also set forth the various field of membership designations available to prospective and existing credit unions. These designations included single occupational, single associational, multiple common bond, or community. Four commenters asked how an existing credit union obtains a charter type designation. Two commenters requested that the credit union be allowed to make its own designation. One commenter requested that a credit union not immediately make a designation, but be provided some latitude until its next examination or when it requests a charter amendment. The Board encourages credit unions to review their charters to determine which designation is most appropriate. NCUA will provide a designation for a credit union when the credit union asks for its first charter expansion under this policy, or upon request by the credit union. If a credit union is unsure of its designation it should contact the regional office. If a credit union disagrees with the designation approved by the region, the credit union can appeal the decision to the Board.

Finally, this chapter sets forth NCUA's long-standing policy prohibiting the establishment of a federal credit union for the primary purpose of serving the citizens of a foreign nation. The Board stated that federal credit unions are permitted to serve foreign nationals within the field of membership when they reside or work in the United States and that foreign nationals may also be served if they reside in a foreign country, but only when the primary purpose of the credit union's foreign service facility is to serve United States citizens who are credit union members residing in the foreign country. Five commenters disagreed with this policy. They believe federal credit unions should be able to serve foreign nationals from the United States who are within their field of membership, even if the foreign national has never resided in the United States. The Board finds these comments persuasive. The Board is retaining its policy of limiting branches outside the United States to locations on U.S. military installations or in U.S. embassies. However, the Board believes that a credit union should be able to serve its entire field of membership no matter where the individual resides. Although there is no legal restriction on such service, there are often legitimate safety and soundness concerns when a federal credit union serves foreign nationals outside the United States. For this reason, the Board is requiring that a federal credit union, wishing to serve foreign nationals within its field of membership and who have never resided in the United States, obtain written approval from the regional director. The credit union will address in its business plan the loan quality, collection and collateral policies involving individuals residing outside the United States. If there are safety and soundness concerns, the regional director may restrict the services a federal credit union may provide to foreign nationals residing overseas. If a credit union is currently serving foreign nationals, they can continue such service until the regional director renders a decision. The credit union has 60 days from the effective date of the manual to send in its request to continue to serve foreign nationals.

II. Chapter 2 of the Chartering Manual

Chapter 2 set forth the field of membership requirements for a federal credit union. This chapter was divided into the following comprehensive sections: (1) single occupational charters, (2) single associational charters, (3) multiple common bond charters, and (4) community charters.

Twelve commenters believed that an occupational group and associational group can be included in a single common bond credit union. One of these commenters believed that the final regulation should expressly authorize that individuals with a common employer can rely on that mutuality of outlook to join the same credit union as individuals belonging to an association which is derived from that employment. One commenter stated that the regulation inconsistently uses the term ''group.'' This commenter stated that, since a single common bond credit union consists of one group, then if NCUA is addressing a subset of a common bond group it should refer to that entity as a subgroup. Eight commenters believed that multiple common bond credit unions should be able to have common bond additions for each group in the credit union's field of

membership. For example, the commenters would argue that, if a multiple common bond credit union has an occupational group in New York in its field of membership and wishes to add a division of that occupational group located in California, then the select group criteria do not apply.

The Board believes that a credit union consisting of an occupational group and a closely tied associational group should be treated as a multiple common bond credit union. Any other interpretation would appear to violate the intent of CUMAA which defines a single common bond credit union as ''one group that has a common bond of occupation or association.'' The Board's intent is that any expansion of a multiple common bond credit union must comply with the multiple common bond rules. It is not intended that a group that has a common bond with a group in a multiple common bond credit union can be added based on the common bond rules. The criteria relative to numerical limitation, reasonable proximity, economic advisability, etc., remain applicable when any new group not previously analyzed is requested to be added. For example, an occupational group with a primary potential membership of 1,000 was previously added to a multiple common bond credit union. The credit union now wants to add all the subsidiaries of the occupational group. In order to add the subsidiaries, they must be independently evaluated to determine compliance with the multiple common bond criteria. Finally, multiple common bond credit unions will not be allowed to circumvent the multiple common bond requirements by repeatedly and methodically adding separate groups within the same common bond.

a. Single Occupational Common Bond Credit Union

The Board proposed that a federal credit union may include in a single occupational common bond all persons and entities who share that common bond without regard to geographic location. The Board stated that eligibility for membership in an occupational common bond can be established in four ways:

- Employment (or a long-term contractual relationship equivalent to employment) in a single corporation or other legal entity makes that person part of an occupational common bond of employees of the entity;
- Employment in a corporation or other legal entity with an ownership interest of not less than 10 percent in or by another legal entity makes that person part of an occupational common bond of employees of the two legal entities;
- Employment in a corporation or other legal entity which is related to another legal entity (such as a company under contract and possessing a strong dependency relationship with another company) makes that person part of an occupational common bond of employees of the two entities; or
- Employment or attendance at a school.

Thirteen commenters were satisfied with an ownership interest of 10 percent. Sixteen commenters recommended the ownership interest should be reduced from 10 percent to 5 percent. Six commenters stated that there should be no limits on ownership interest. The Board is retaining the 10 percent ownership interest requirement. There are other federal regulations setting forth 10 percent ownership as a rationale presumption for control of another entity. For example, the Federal Reserve Board presumes that when one company owns 10 percent of the voting securities of a state member bank or bank holding company, the 10 percent ownership constitutes the acquisition of control under the Bank Control Act. 12 CFR Section 225.41(c)(2).

Thirty-three commenters suggested that NCUA's approach to occupational common bond cover other possible relationships among corporations such as franchise relationships. Five commenters opposed including franchisee relationships as part of an occupational common bond. Franchise relationships may be part of an occupational common bond depending on whether there is any contractual or dependency relationship with the occupational group. However, this test is fact specific so NCUA cannot set forth a general rule that all franchises are part of a single occupational group.

Thirty-one commenters recommended that NCUA's approach to common bond include other types of common bonds, such as all schools in an area, or all health care facilities, or public safety employees and one of these commenters stated that these common bond groups be specifically named in the credit union's charter. A majority of these commenters stated that NCUA should be more flexible in defining an occupational common bond. For example, one commenter requested that occupational groups such as electricians, plumbers, and taxicab drivers should be defined as an occupational group. Seven commenters opposed expanding the occupational common bond to include all schools in the area, or all health care facilities or public safety employees. It appeared that a majority of these commenters requested that NCUA establish a policy that was first promulgated in IRPS 96–2. That policy recognized a fourth definition of occupational common bond based on a trade, industry or profession (''TIP'').

In First National Bank and Trust Co., et al. v. *NCUA*, the U.S. Court of Appeals for the District of Columbia Circuit recognized that in some respects NCUA's chartering and field of membership policies may be more restrictive than required by the FCUA. That is, NCUA may identify and approve interpretations that provide broader common bonds than presently permitted. Moreover, given the Court of Appeals determination that the mere element of ''resemblance or common characteristic'' in the definition of groups is the equivalent of a common bond, NCUA clearly has very broad discretion in defining what constitutes a common bond for purposes of federal credit union membership.

CUMAA defines a single common bond credit union as ''one group that has a common bond of occupation or association.'' While the term ''occupation'' is consistent with the Court of Appeals finding, for the purposes of this rule, the Board has decided to again adopt a definition that is more restrictive than that permitted by statute. For the most part, a single occupational credit union is based on employment and any contractual, ownership and dependency relationships to that employment. The decision to not propose a TIP policy is based on operational concerns and the fact that when credit unions were allowed to expand using multiple common bond policies it did not appear that a broader definition was necessary. However, while the Board is not adopting a TIP definition of occupational common bond at this time, the Board's view is that such a policy is legal and may again be proposed after evaluating the impact and effectiveness of the current multiple common bond policy.

One commenter stated that employees and students at a school do not share an occupational common bond. Three commenters stated the occupational common bond for a school should be expanded to include multiple schools. Although the Board believes that employees and students at a school clearly share the same common bond, it does not believe the same is true for multiple schools. Each school is separately organized and chartered and the employees and students at one school may not necessarily share the

same common bond with another school. For example, the employees and students at the University of Buffalo do not share a common bond with the employees and students at the University of Texas. However, employees in schools supervised by the same school district or board of education may share an occupational common bond.

Two commenters requested that a group that has a contractual relationship with an occupational group be considered part of one occupational group. One commenter stated that government contractors of government agencies should be considered part of the occupational common bond. The Board, as stated above, permits contractors to be part of a single occupational common bond provided they have a contractual and strong dependency relationship with the group.

Five commenters requested that the tenants of individual parks, shopping malls and office complexes and their employees should be considered to have a common bond of employment. NCUA cannot define an occupational common bond based on location—it must be based on the statutory requirement of occupation. Therefore, the final rule does not include this type of occupational common bond. However, industrial parks, shopping malls, etc., may qualify as a community charter.

A few commenters questioned whether a single occupational common bond credit union, after adding one new group, could still serve its sponsor group outside the service area. The Board believes the credit union can continue to serve its sponsor group outside the service area. However, the credit union then becomes a multiple common bond credit union and service area requirements apply to any new groups the credit union wishes to add.

A number of commenters objected to providing a geographical description for single occupational common bond credit unions. NCUA has historically provided a geographic definition for single occupational common bond credit unions because more than one credit union may be serving different divisions of the same company. Additionally, overlap concerns, other than incidental overlaps, still must be resolved. While there are no geographical limitations for federal credit unions, a federal credit union must still specify its geographic definition, which can be located throughout the United States.

Occupational Common Bond Amendments. The proposed rule set forth when NCUA would approve an amendment to expand a credit union's field of membership. Specifically, the Board addressed the situation where the sponsor organization is involved in a corporate restructuring. The Board stated that a credit union could continue to provide service to a group that is spun-off only if it otherwise qualifies as part of the single occupational common bond, or if the credit union converts to a multiple common bond credit union. Six commenters stated that, if a business sells or spins off an operating unit or subsidiary, both current and future employees of the operating unit or subsidiary should remain eligible for membership in the occupational credit union without having to convert to a multiple common bond credit union. The Board does not find these comments persuasive. If a company spins off a group that the credit union was serving, the credit union will be able to continue to serve the group if the credit union converts to a multiple common bond charter. If the credit union wishes to expand, it must follow the multiple common bond expansion policies.

The Board set forth a second instance requiring an amendment when the entire field of membership is acquired by another corporation. The credit union can serve the employees of the new corporation, including any subsidiaries of the acquiring corporation, after receiving NCUA approval. The Board stated that, in this instance, the credit union remains a single common bond credit union.

One commenter opposed a conversion process if a single common bond credit union wishes to become a multiple common bond credit union. This commenter believed that, if a credit union added an unlike group to its field of membership the credit union has converted to a multiple common bond credit union. The Board believes that a credit union that wants to serve multiple common bonds should formally convert its charter. Accordingly, the final regulation sets forth this process.

b. Single Associational Common Bond Credit Union

The proposal set forth the definition of associational common bond. The Board stated that an associational common bond consists of individuals (natural persons) and/or groups (non-natural persons) whose members participate in activities developing common loyalties, mutual benefits, and mutual interests. This would permit an associational common bond to include members of the association, groups which are not comprised primarily of natural person members but are members of the association, and employees of the association, as well as the association. The proposal also stated that an associational charter may be granted without regard to the geographic location of the association's members or headquarters. This means a credit union could serve a widely dispersed membership base if NCUA determines that it has the ability to serve the area.

One commenter requested that public housing residents be treated as an associational common bond. Public housing residents, who simply are in the same location, do not meet NCUA's associational common bond requirements. Public housing residents must be part of a bona fide association to be considered an associational group.

The Board also stated that associations based primarily on a client-customer relationship would not meet associational common bond requirements. For example, members of an automobile club, such as the American Automobile Association, which primarily sells services, would not qualify as an associational common bond. The Board is adopting this policy in the final regulation.

The Board further stated that the alumni of a school must first join the alumni association, and not merely be alumni of the school to be eligible for membership. One commenter objected to this provision because in some schools the graduates are automatically members of the alumni association. If an alumnus is automatically a member of the alumni association because the individual graduated from that college, then the person is considered part of the associational common bond. However, in most cases, the person must satisfy membership requirements of the alumni association, such as paying dues or participate in alumni activities, to be eligible for credit union membership based on an associational common bond. One commenter stated that an alumni group and a college group share the same associational common bond. The Board disagrees. The interests of the alumni association and the interests of the students at the university are often divergent.

Finally, the Board stated that, if an association subsequently changes its bylaws, the credit union cannot serve the new members of the association until NCUA approves the revised charter and bylaws through a field of membership amendment. The Board is adopting this policy in the final regulation.

Corporate Restructuring. Due to a corporate restructuring of a select group,

a credit union may be required to request an amendment to its field of membership if it wishes to continue to provide service to that group. The Board proposed to permit an associational credit union to continue to serve the group if it was still part of the associational common bond or the credit union converts to a multiple common bond credit union. Three commenters stated that the associational credit union should be able to continue to serve the group regardless of common bond requirements. The Board does not find these comments persuasive. If an association spins off a group that the credit union was serving, the credit union will be able to continue to serve the group if the credit union converts to a multiple common bond charter. If the credit union wishes to expand, it must follow the multiple common bond expansion policies.

One commenter stated that, if an associational common bond spun-off part of the association, the final rule should clarify that relatives of existing members of the credit union belonging to the sold or spun-off group could continue to be eligible for membership in the credit union. Immediate family members of existing credit union members are still eligible for membership even if the group is no longer in the credit union's field of membership provided that the credit union does not further restrict family member eligibility. This rationale has universal application to all charter types.

c. Multiple Common Bond Credit Union

Five Statutory Criteria. Before a credit union can add a new occupational or associational select group, NCUA must determine in writing that five statutory criteria have been met. The first criterion is that the credit union did not engage in any unsafe or unsound practice which is material during the one-year period preceding the filing of the application. The Board defined an unsafe or unsound practice for this criterion to mean any action, or lack of action, which would result in an abnormal risk or loss to the credit union, its members, or the NCUSIF. The Board stated that the determination of an unsafe and unsound practice would be decided by the regional director. Two commenters requested further guidance on what is an unsafe and unsound practice. The Board's view is that additional clarification may unduly restrict the regional director's ability to properly ascertain if a safety and soundness concern exists. Obviously, what is a safety and soundness concern for one credit union may not be for another credit union because of a credit union's size, resources, management expertise, etc.

The second criterion is that the credit union is adequately capitalized. The Board defined adequately capitalized to mean the credit union has a net worth ratio of not less than 6 percent. The Board also specifically requested comment on what criteria should be considered when defining ''adequately capitalized'' for newly chartered credit unions.

Thirty-four commenters stated that they approved of the definition or that requiring a net worth of 6 percent in order to add select groups would not place an unreasonable burden on their credit unions. One commenter stated that there should be no minimum capital adequacy requirements for new or low-income credit unions wishing to expand their charters.

Twenty-five commenters opposed the definition and some of these commenters stated that requiring a net worth of 6 percent would place an unreasonable burden on credit unions. Many of these commenters stated that CUMAA does not require the 6 percent level. Two commenters stated that, if the Board determines that it is necessary to retain the 6 percent capital requirements for group additions then they encourage the Board to consider as part of its economic advisability determination whether the addition will actually raise the credit union's capital. These commenters stated that such an addition should be permitted if the expansion increases capital to at least 6 percent within a reasonable period of time. These commenters also stated that a credit union with a capital of less than 6 percent should be allowed to bring in a group as part of a sanctioned net worth restoration plan. Twelve commenters stated that adding new groups may be the best way for an undercapitalized credit union to obtain an adequate capitalization level. Three commenters stated that NCUA should be flexible in defining adequately capitalized.

In 1982, the Board decided that multiple groups could be joined together through the chartering process, amendment of the charter, or by way of merger to form a single credit union. A major reason for the policy change was to provide small groups of people, who did not have the ability to charter their own credit unions, access to credit union service. Another reason for the policy change was to assist credit unions in diversifying their fields of membership for safety and soundness reasons. The rationale applicable in 1982 remains applicable today. For that reason, the Board included in the final rule for single common bond and community credit unions the possibility that an expansion could be approved notwithstanding the credit union's financial or operational problems.

CUMAA, however, requires a different standard for multiple common bond credit unions in that it requires the credit union to be adequately capitalized before an expansion can be approved. As of June 1998, the average net worth ratio for all federal credit unions was 13.55 percent. Of the 6,907 federal credit unions, 39 percent were above the average and 61 percent were below. More importantly, only 4 percent, or 269 federal credit unions, would not now meet the 6 percent adequate capitalization requirement. It is the Board's view that a 6 percent capitalization for field of membership expansions for multiple common bond credit unions chartered more than 10 years is reasonable and establishes a standard that, while not meeting the average capitalization level of federal credit unions, is indicative of a credit union that generally is managed in a safe and sound manner. Additionally, although not required by CUMAA to set the capitalization level at 6 percent, such a percentage ties to the capitalization level established for prompt corrective action. However, the Board believes that a newly chartered multiple common bond credit union, chartered less than 10 years, or a low-income credit union, may obtain a field of membership expansion even though its capitalization level is less than 6 percent if the credit union, as determined by the regional director, is making reasonable progress toward meeting the 6 percent capitalization level.

The Board believes that a restoration capitalization plan, which was a basis for the 1982 policy and which remains operationally desirable, is not consistent with the statutory requirement in CUMAA that, before an expansion can be granted, the credit union must be adequately capitalized. A capitalization restoration plan, while operationally desirable, could essentially render the statutory requirement that the credit union be adequately capitalized meaningless. A ten-year window to obtain a capitalization level of 6 percent is reasonable, obtainable and consistent with prudent safety and soundness goals.

The third criterion is that the credit union has the administrative capability and the financial resources to serve the proposed group. To determine whether the credit union has met this criterion, the Board stated that it would review

the credit union's most recent examination report or, if necessary, contact the credit union directly. Two commenters stated that there should not be any undue requirement under this criterion for small groups. The Board simply expects a credit union adding new groups, regardless of the size of the group, to demonstrate how it will serve the group. The larger the group, the greater the burden the credit union has to show that it can serve that group. In approving new select groups, the regional director has the discretion in requesting documentation on how well the credit union is serving its current field of membership.

The fourth criterion is that the credit union must demonstrate that any potential harm the expansion may have on any other credit union and its members is clearly outweighed by the probable beneficial effect of the expansion. The Board stated that the agency will perform an overlap analysis to determine whether this criterion has been met.

Thirty-two commenters believed this test is useful. Most of these commenters believed overlaps help the consumer. Twelve commenters opposed this statutory criteria. Most of these commenters believed overlaps are good for the member. A number of these commenters requested NCUA to base decisions on potential harm on objective criteria. Twelve commenters questioned how the convenience and needs of the members will be quantified and measured. One commenter stated that if the two credit unions agree to the overlap, then NCUA should find no harm to the overlapped credit union. Some of these commenters suggested that a measurement of ''convenience and needs of the members'' should include new or expanded products/services which are not offered by the other credit union as well as increased access to the credit union through fixed service sites, mobile sites, extended service hours and 24 hour electronic media. In response to the comments regarding the measure of the convenience and needs of the members, NCUA will review the products, services and service delivery methods offered by the overlapping credit union. NCUA will measure potential harm to the overlapped credit union as a threat to its solvency. A recent NCUA study determined that overlaps, as a general rule, will not adversely affect the overlapped credit union. Therefore, in most cases, NCUA will probably find that the convenience and needs of the members will outweigh the harm to the overlapped credit union. This suggestion of probability, while not conclusive, is based on experience.

An expanding credit union has the duty to investigate whether an overlap exists. Many of the commenters that opposed the criterion did not believe the credit union should investigate whether an overlap exists. A few commenters suggested that an expanding credit union discharges this duty by asking the group whether it receives services from other credit unions. The Board agrees with these comments. As long as the expanding credit union has, in good faith, documented that the group does not have other credit union service, it will not be penalized if an overlap is discovered at some later time. However, the group may be removed from the expanding credit union's field of membership.

The fifth criterion is that NCUA must determine that the formation of a separate credit union is not practical or does not meet the economic advisability criteria. Four commenters requested more guidance on how to determine whether forming a separate credit union is practical. A few commenters suggested that when evaluating this criterion, NCUA should determine whether the independent credit unions can be full service and offer share drafts, ATM cards, etc. The Board will look at the desire of the group, the services it can provide and its economic advisability before deciding whether to allow a group with under 3,000 primary potential members to join the credit union. If the group does not wish to form its own credit union, does not have the volunteers and resources to charter a credit union, and is otherwise not economically advisable, NCUA will allow the group to join an existing credit union. Although some commenters did not believe this criterion was necessary for groups under 3,000, it is consistent with the statutory language and congressional intent. If the group is 3,000 or more primary potential members, the desire of the group, while important, must be weighed against the statutory criterion that the group cannot feasibly or reasonably establish a single common bond credit union.

One commenter asked whether NCUA has to make a formal determination on all five criteria when adding a group to a credit union's field of membership. Four commenters stated that a written determination is not always required, as in the case of ''successor'' groups. The Board believes it does not have the discretion to waive a written determination. However, in those cases where there is no overlap and the group is small, the written determination should be processed expeditiously. A ''successor'' group would not be treated as a select group expansion, rather it is treated as a housekeeping amendment and, therefore, a written determination is not necessary.

While all federal credit unions are encouraged to expand their service to underserved areas, the Board especially encourages multiple common bond credit unions that add new groups to consider service to underserved areas. The Board believes that multiple common bond credit unions are uniquely positioned, because of their service delivery systems, to provide credit union service to such areas.

3,000 Numerical Limitation. The proposal also set forth the requirements for adding a group in excess of 3,000 primary potential members to a credit union's field of membership. One commenter asked whether it is permissible to add the employees of a sponsor (which has total employees exceeding 3,000) working in a specific geographic area, if the number of employees in that area is less than 3,000 (i.e., can sponsors be segmented to meet the requirement applicable to the number of employees). Two commenters supported NCUA's interpretation of the numerical limitation. One commenter questioned whether the 3,000 number is potential new members or that the group itself has no more than 3,000 total members. The 3,000 numerical limitation is based on the current number of employees or members of the group. Five commenters stated that the wishes of the group and sponsor should be key factors for NCUA to review in making its determination as to whether a group can be added. Although NCUA agrees with these comments that these are key factors, they are not conclusive.

Three commenters opposed the statutory 3,000 numerical limitation. Some commenters requested more specific criteria on when a group of 3,000 or more would be approved as an addition to an existing multiple common bond credit union. The Board believes that such an addition is determined on a case-by-case basis consistent with the statutory requirements. NCUA will look at the size of the group (is the group 100,000 or 3,000), desires of the group, the volunteers and resources to support the efficient and effective operations of the credit union, whether the group meets the economic advisability criteria and the demographics of the group. A few commenters asked whether a letter from the CEO of the company stating that it does not wish to form a new credit union and does not have volunteers and

resources to start a new credit union is sufficient. Although such a letter is persuasive evidence, NCUA will look at the totality of the evidence surrounding the request.

Documentation Requirements. The proposal set forth the documentation requirements to add a select group and NCUA's procedures for amending the field of membership. One commenter believed that NCUA should not require a letter from an authorized representative of the group to be added. This commenter suggested that if the credit union cannot get a letter from an authorized representative that a petition from the group should be acceptable. NCUA agrees and the final rule allows the regional director to accept other documentation as appropriate.

Streamlined Procedures. Seventy-three commenters requested NCUA adopt a streamlined application program for the addition of small employee groups. Two commenters did not support a streamlined approach. Twenty commenters requested that NCUA reinstate the Streamlined Expansion Procedure (SEP). The Board cannot reinstitute SEP because CUMAA requires a written determination by NCUA before a group is added to a credit union's field of membership. Three commenters stated that groups added under SEP be included in the credit union's current charter. The Board agrees and the SEP log will be made part of the official credit union charter.

The Board has developed an expedited process for groups of 200 or less primary potential members. Although a written determination regarding the listed regulatory and statutory criteria is still required, the processing of small groups will be accomplished more expeditiously by the region through the use of the Form 4015–EZ.

Eighteen commenters requested that the regional director respond to multiple common bond expansion requests within a specific time frame. Although the Board is not setting a definitive time frame for rendering a decision, it expects the regions to make a decision expeditiously upon receipt of a completed application.

Distressed Designation. Under IRPS 94–1, a credit union could apply for a distressed designation that eliminated certain field of membership restrictions for the applicant credit union. No credit union ever applied for the designation. Two commenters requested that NCUA reinstitute the distressed designation so that a credit union could add groups regardless of location or common bond. The Board does not believe there is a need for such a policy. Additionally, the Board believes that CUMAA does not provide NCUA with the latitude to institute such a policy.

Corporate Restructuring. Due to a corporate restructuring of a select group, a credit union may be required to request an amendment to its field of membership if it wishes to continue to provide service to that group. The Board proposed to permit a multiple common bond credit union to retain in its field of membership a sold or spun-off group to which it has been providing service, without regard to location, if the original group is clearly identifiable and requests continued service. The Board stated that it views this as a housekeeping amendment and not a field of membership expansion. Eight commenters specifically supported this position. Two commenters stated that the policy should encourage a company to provide a signed letter requesting service but that it doesn't need to be a requirement. Two commenters stated that in a corporate restructuring no new overlap analysis is necessary. The Board agrees with all these comments and will treat such corporate restructuring amendment requests as a housekeeping amendment and no overlap analysis is required. Furthermore, the Board is no longer requiring a letter from the company requesting service. Finally, a name change is not a corporate restructuring, but the credit union should obtain a housekeeping amendment to update its charter.

Branching. Under IRPS 94–1, a credit union could justify a new branch by adding groups within the branch's operational area as long as a significant portion of the total number of persons to be served by the facility when it opened were from the field of membership that existed prior to adding the select groups. Although ''significant portion'' of the field of membership was not defined, the intent behind the policy was not to encourage federal credit unions to establish branches simply for the purpose of adding groups. In practice, NCUA viewed as few as 300 members to be a significant portion of the field of membership for the purpose of branching. NCUA's current proposal does not have any limitations on when and where a credit union could branch. Hypothetically, a multiple common bond credit union could branch in an area where it has no current members. One commenter disagreed with this provision and stated credit unions can only branch where they have existing members. Seven commenters requested that NCUA allow groups to be added to a credit union's field of membership before they even establish a service facility in the area. Although the Board does not have many restrictions on branching, the Board does not agree with these commenters. The Board's view is that CUMAA requires a service facility be established before a credit union adds a group not currently within its service area. Groups cannot be added in anticipation that a service facility will be established. That is, a credit union that intends to expand into a geographical area not currently served by the credit union, must first establish a service facility. Once the service facility is established, then the credit union can add groups that are within the service area of that service facility.

Conversions. The proposal stated that a multiple common bond federal credit union may apply to convert to another type of charter provided the field of membership requirements of the new charter type are met. Groups that do not qualify in the new charter type cannot be served, only members of record from those groups. Furthermore, the Board has established a process for multiple common bond credit unions converting to single common bond credit unions. One such requirement would not permit the credit union to convert to another type of charter, except a community charter, for 3 years after approval, unless the regional director determines that a charter conversion is necessary to resolve safety and soundness concerns. Additionally, the credit union must notify the groups that will no longer be served. This notification requirement also applies to single common bond credit unions converting to community charters. Community credit unions converting to single or multiple common bond charters are exempt from the notification requirements.

One commenter suggested that groups acquired through an emergency merger can continue to be served after the charter is converted. The Board agrees and the final regulation exempts groups or communities that were acquired through an emergency merger or purchase and assumption agreements.

d. Community Charters

CUMAA requires that a community charter be based on ''a well-defined local community, neighborhood, or rural district.'' The Board set forth the following requirements for a community charter:

- The geographic area's boundaries must be clearly defined;
- The charter applicant must establish that the area is a well-defined ''local community, neighborhood, or rural district;'' and
- The residents must have common interests or interact.

The Board proposed that ''well-defined'' means the proposed area has specific geographic boundaries. The Board also stated that a ''local community, neighborhood, or rural district'' encompasses several factors including interaction and/or common interests. Although the proposal did not precisely define interaction or common interests, it did suggest that a greater burden needs to be met when either the geographic size or the population of the area is large. The Board stated that in determining interaction and/or common interests, a number of factors become relevant. For example, the existence of a single major trade area, shared governmental facilities, local festivals, area newspapers, among others, would be significant indicia of community interaction and/or common interests. Conversely, an area which has numerous trade areas, multiple taxing authorities, or multiple political jurisdictions would tend to diminish the factors that demonstrate the existence of a local community, neighborhood or rural district.

Comments. It was clear that many of the commenters confused the standard community chartering policy with the requirements for a streamlined approach to obtaining a community charter. Thirty-five commenters stated that NCUA's approach to the definition of ''local community'' provides sufficient guidance for credit unions that might be seeking a community charter. Seven commenters specifically approved of the requirement that the residents of the proposed community either interact or have common interests. One commenter requested further standards for interaction. One commenter opposed the interaction and common interest standards. One commenter stated that the interaction requirement does not take into account sparsely populated rural areas. One commenter encouraged the Board to strengthen the language in the final rule that concentrates on interaction and confluence of interest within an area as the most important test of whether the requirements for a community have been met, rather than the size of any particular area. A number of commenters provided suggested definitions for a local community.

Six commenters stated that NCUA's community policy should be flexible for sparsely populated areas. For example, these commenters stated that a rural multiple-county area should be considered a local community. Two commenters stated that the definition needs to be flexible when drawing the boundaries of a well-defined community. A few commenters suggested that the Board should recognize that what constitutes a community in California might be significantly different from what constitutes a community in South Carolina or Alaska.

Thirteen commenters disagreed with NCUA's approach to the definition of ''local community.'' Five commenters stated the definition is too restrictive. Four commenters stated NCUA's definition of local community needs to be more specific. Three commenters stated that large metropolitan cities should be considered as local communities. One commenter stated that a state might qualify as a local community. Two commenters stated that multiple counties should not constitute a local community.

NCUA Board Analysis and Decision on Community Charters. CUMAA modified NCUA's community chartering policy. It requires that a community charter be based on ''a well-defined local community, neighborhood, or rural district.'' Although Congress did not provide specific guidance on what constituted a ''local community, neighborhood or rural district,'' the Board concluded that the addition of the word ''local'' to the previous statutory language was intended as a limiting factor and that additional clarification was required relative to what would qualify as a community charter. The Board further concluded that a more circumspect and restricted approach to chartering community credit unions appeared to be the congressional intent. Accordingly, recognizing that ''local'' was a limiting factor, NCUA staff reviewed those community charter applications approved by the Board in the last three years in an effort to more narrowly define what will constitute a community charter based not only on operational feasibility, but also historical data that tended to support whether a particular well-defined area would qualify as a local community, neighborhood or rural district.

Although the proposal did not completely define interaction or common interests, the Board stated that in determining interaction and/or common interests, a number of factors, are relevant. The Board continues to believe those factors remain valid. These factors are limiting in the sense that they clearly require a community charter applicant proposing to serve multiple trade areas, etc., to demonstrate more definitively how it meets the local requirement. The Board believes that increased documentation requirements need to be met when either the geographic size or the population of the area is large.

The Board stated that, in general, a large population in a small geographic area or a small population in a large geographic area, may meet community chartering requirements. Conversely, the Board stated that a large population in a large geographic area will not normally meet community chartering requirements. In so doing, however, the Board has not summarily dismissed or prejudged any potential application. While an area with a large population may require additional documentation, it still may meet the definition of a local community. Similarly, multiple counties, particularly in rural areas, may qualify for a community charter.

One commenter stated, ''[t]herefore, no geographic size area and no population size is ruled out—all are fair game, subject only to NCUA's discretion. So, effectively, there is *no* geographic or population size limitation for the chartering of community credit unions in the NCUA proposal.'' The commenter correctly interpreted the proposal relative to geographic and size limitations, but failed to acknowledge the overriding requirement that, regardless of the size, the proposed community area must meet the ''local'' standard that Congress directed NCUA to develop. NCUA's responsibility is to review community charter applications to ensure this statutory requirement is satisfied. Accordingly, the Board believes the proposed definition properly incorporates the congressional intent with the need to provide opportunities for community charters. Except for the addition of some clarifying language, the Board is adopting the proposed policy in final.

Two commenters asked if multiple but separate, well-defined areas could comprise a local community charter. This is not statutorily permitted. The entire area must be a single well-defined location. Two, noncontiguous, well-defined areas cannot be the basis for a community charter.

The Board also stated that a low-income area meeting the low-income definition found in Section 701.34 of NCUA's Regulations has many of the common characteristics and demographics of a local community, and generally lacks the basic financial services found in more affluent communities. 12 CFR 701.34. The Board proposed that, when reviewing low-income community charter applications, NCUA's documentation requirements would be more flexible and fewer documentation requirements would be required than for a standard community charter package. There was no significant objection to this provision.

The Board is adopting this proposal in the final regulation.

Presumptive Community. The Board also proposed a streamlined community chartering process for a well-defined local community, neighborhood, or rural district where the area to be served is a recognized political jurisdiction, not greater than a county or its equivalent, and the population of the requested well-defined area does not exceed 300,000. The Board stated that, generally, the single jurisdiction will most often coincide with a county, or its political equivalent. Multiple contiguous smaller political subdivisions within a county or its equivalent, such as a city, township or a school district, would also qualify under this proposal. The Board proposed that for this type of community charter, the applicant must only submit a letter demonstrating how the area meets the indicia for community interaction or common interests. In addition, the applicant would have to provide evidence of the political jurisdiction and size of the population.

The Board further stated that, at its discretion, NCUA may request more documentation demonstrating the area is a well-defined local community, neighborhood, or rural district. If the requested area is not a single political jurisdiction or exceeds 300,000, more detailed documentation would have to be provided to support that the proposed area is a well-defined local community, neighborhood or rural district. The Board also stated that community charters were not limited to a recognized single political jurisdiction, or to a proposed area where the population is 300,000 or less. Simply, additional documentation, as required for standard community charters, would be required if the proposed community charter exceeds an area greater than a county or 300,000 in population. In other words, the definition of local community may include not only those that qualify under the presumptive factor, but also other local well-defined areas meeting the community charter requirements. The Board specifically requested comment as to whether a streamlined approach for community charter approval is appropriate and, if so, in accordance with what criteria.

Comments. As stated earlier, many commenters confused the presumptive community with the standard community chartering policies. Again, a local community is not limited to a single political jurisdiction with a population of 300,000 or less.

Thirty-eight commenters approved of the limited documentation requirements for community charter applications that are within a single political jurisdiction and have 300,000 or less in population. One commenter stated that the size of the population should not matter and that the streamlined procedure should be available for any community charter request that does not exceed a single political jurisdiction not larger than a county or its political equivalent. Nineteen commenters suggested that other types of communities should also have limited documentation requirements, with many of these commenters stating that multiple counties should also be a part of the streamlined documentation requirements. Two commenters stated, that if the community consists of multiple counties, then NCUA should lower the population requirements.

Six commenters suggested a higher population threshold. One commenter suggested that the population size be increased to 500,000. Two commenters suggested that the population size be increased to one million. One commenter stated that the population size should be up to one million and include multiple counties. Six commenters would eliminate any population size. Sixteen commenters generally disapproved of the streamlined approach as proposed. Two of these commenters stated that the population size and political jurisdiction should simply be taken into account when considering the application but should not be the deciding factors. Some commenters were opposed to the 300,000 limit for a streamlined approach either because the number was too large or too small.

One commenter wondered whether it was a concern if the proposed community area was located in two different states. It depends on the facts but, conceptually, a community could cross political jurisdictional boundaries and still qualify for the streamlined approach. For example, a town that is in parts of two counties and has a population 300,000 or less would qualify for the streamlined approach.

NCUA Board Analysis and Decision on Presumptive Community. The NCUA Board is adopting the presumptive community as initially proposed. Additionally, the Board is adopting a second method based on multiple contiguous counties or multiple political subdivisions thereof with a lesser population threshold by which a presumptive community can be established. As to the initial proposal, the Board is limiting the streamlined approach to communities contained in a single political jurisdiction where the population does not exceed 300,000. The Board is not raising the population threshold because experience has demonstrated that a single political jurisdiction of this size, or less, has the normal indicia for community chartering.

Relative to the second method, the Board is also of the opinion that multiple contiguous counties, or multiple political subdivisions thereof, will most likely have the normal indicia for community chartering, particularly in rural localities, if the population of the well defined area does not exceed 200,000. In both instances the presumption is rebuttable, and the regional directors may require additional evidence to support the local community, neighborhood or rural district criteria. The Board may revisit this issue in the future if more experience with larger communities is obtained by NCUA.

In setting forth the example of a ''county'' with a population of 300,000 or less as a presumptive community, the Board was simply providing guidance and setting a maximum geographic limit for the streamlined process. A state or a congressional district would not qualify for a presumptive community. However, for purposes of the streamlined approach, a political jurisdiction that is less than a county would qualify. For example, a municipality or a city would qualify as a single political jurisdiction for the streamlined approach if the population of the municipality or city does not exceed 300,000.

Some commenters asked for NCUA's rationale for establishing the presumptive community at 300,000. The Board's rationale for this number is based on the Board's review of its historical actions in granting community charters. In every case where the community was 300,000 or less and contained in a single political jurisdiction, the Board found that the particular area would qualify as a local community, neighborhood or rural district.

Credit Unions Converting to Community Charters. The Board stated that a credit union converting to a community charter must contact all federally insured credit unions in the area regarding the potential overlap. A few commenters requested that this requirement be eliminated due to the burden placed on the community credit union. The Board agrees, and it is no longer required.

The Board stated that a credit union that converts to a community charter may continue to serve existing members

of the credit union who are not within the community, under the statutory provision that once a person becomes a credit union member, he or she can remain a member. However, the Board stated that a community credit union would not be able to add new members from those groups in the previous field of membership that are outside the community boundaries or add new groups outside the community boundaries. Members of record, outside the community boundaries, could still be served by the community charter. Three commenters approved of NCUA's position. Twenty commenters requested that all groups outside the community boundary should continue to be served by the community credit union. Two commenters requested that, in a conversion to a community charter, NCUA permit the credit union to continue to serve its original sponsor even if the original sponsor is outside the community boundaries. The Board believes that when a credit union converts to a community charter it should serve the community and not select groups. Serving groups outside the community boundaries is not indicative of a community charter. The only exception is for groups obtained through an emergency merger or emergency purchase and assumption. The grandfather provision in CUMAA is not applicable since the credit union has changed its charter type.

The proposed rule on community charters specified that ''[c]ommunity credit unions will be expected to follow, to the fullest extent economically possible, the marketing and/or business plan submitted with their application. The community credit union will be expected to regularly review its business plan as well as membership and loan penetration rates throughout the community to determine if the entire community is being adequately served.'' Four commenters believed this requirement is reasonable. Six commenters stated that, in reviewing a community credit union's business plan, NCUA should consider the credit union's good faith efforts to comply with its plan and not just focus on the extent to which the credit union is achieving the plan. Thirteen commenters strongly objected to the inclusion of this language, particularly the reference to membership and loan penetration rates. It is their position that the language would impose Community Reinvestment Act (CRA) standards, and that Congress clearly has had no such intent. When this language was first developed in 1997, it was not the intent to impose CRA standards. The intent was to simply outline the expectation that community charters are chartered to serve the entire community, just like any other charter type should attempt to serve their field of membership, and not a portion of the approved well-defined area, and that the business plans should reflect this goal. That is the nature of a community charter. Finally, with respect to the proposed language, it was never intended that additional examination or supervisory controls would be required. At the time this language was under consideration, there was considerable evidence that the number of community charter applications would increase due to the adverse court rulings. Again, the objective was to reiterate that community charters should make every effort to serve the community, and not just those groups already in the converting credit union's field of membership. However, to further clarify the Board's position, the Board has modified the language to read as follows: ''Community credit unions will be expected to regularly review and to follow, to the fullest extent economically possible, the marketing and business plan submitted with their application.''

Mergers. The proposal stated that a community credit union cannot merge into a multiple common bond credit union except in an emergency merger. Three commenters stated that a community charter should be allowed to merge with a multiple common bond credit union. It remains the Board's view that community charters should not be allowed to merge into multiple common bond charters, absent emergency merger criteria. If a multiple common bond credit union merges into a community charter, the community charter may only serve new members of groups that are located within the community charter boundaries. Of course, the continuing credit union can retain members of record under the ''once a member, always a member'' policy.

Applications In Process. The Board has determined that all community charter applications that were submitted prior to August 7, 1998, and are still outstanding, must be finally submitted with all required documentation to the regions by June 30, 1999, in order to be processed pursuant to the community policies set forth in IRPS 94–1. If a completed community charter application package is not received by the regions by June 30, 1999, then it will be necessary to process the application consistent with IRPS 99–1.

e. Changes Applicable to All Federal Credit Unions

Removal of Groups. The proposal set forth the procedures for a credit union, with NCUA approval, to remove groups from a credit union's field of membership. One commenter stated that this section needed to be clarified so that, if a group is removed from a credit union's field of membership, current members retain membership. The Board agrees. If a group is removed from a credit union's field of membership, current members retain membership under the ''once a member, always a member'' policy. This rationale applies to all charter types.

Appeal Procedures. The regulation sets forth certain appeal procedures. Unless the credit union is requesting reconsideration, it has 60 days to appeal a denial. One commenter requested 90 days to appeal and 60 days to provide supplemental information in a reconsideration. Two commenters asked how long NCUA has to respond to an appeal and one of these commenters stated that the appeal process favors NCUA.

The Board believes that a 60-day time frame gives the credit union sufficient time to appeal the region's determination. The Board's recent experience leads it to believe flexibility is necessary in deciding appeals. Although the appealing credit union may want an expeditious decision, most importantly, it wants a correct decision. The Board, therefore, is not setting a definitive time frame for rendering a decision on appeal, but will attempt to notify the appellant any time a decision cannot be reached within 90 days. The Board is cognizant of the need for an appellant to receive a decision as soon as reasonably possible. Accordingly, every effort will be made to expeditiously process and consider all appeals.

In general, credit unions can appeal adverse decisions by the regional director, including decisions regarding exclusionary clauses. Except for this modification regarding exclusionary clauses, the Board is adopting the proposal in final.

Emergency Mergers. The Board issued clarifying language regarding emergency mergers and purchase and assumption agreements for occupational, associational and community charters. Among other minor modifications, the Board proposed to remove the 12 month period within which insolvency must occur, since it is not required by the FCUA. One commenter approved of this entire provision. One commenter approved of the removal of the 12

month insolvency period. One commenter requested that a multiple common bond or single common bond credit union that takes in a community area as the result of an emergency merger or purchase and assumption should be able to expand the community portion of its charter. The Board disagrees with this suggestion and is adopting a policy that community fields of membership acquired through emergency mergers cannot be the basis of an expansion since the character of the acquiring credit union has not changed. The Board is adopting the proposed emergency merger provisions in final and would like to emphasize that, in the coming year, consistent with legal advice, credit unions not making acceptable progress in becoming Y2K compliant may be determined to have serious and persistent operational problems requiring expeditious action.

Once a Member Always a Member. CUMAA permits any person or organization, who is a member of any federal credit union at the date of enactment, unless expelled under Section 118 of the FCUA, to maintain membership in the credit union. This provision codifies the ''once a member, always a member'' policy. The Act also permits a member, or subsequent new member, of any group whose members constituted a portion of the membership of any federal credit union at the date of enactment, to continue to be eligible for membership in the credit union. For example, an employee of a select group who was eligible for membership prior to August 7, 1998, but did not join the credit union, is still eligible to join the credit union. This also applies to new employees hired subsequent to the date of enactment. Twelve commenters approved of the ''once a member, always a member'' policy.

Twenty-five commenters disapproved of the proposed ''once a member, always a member'' policy. Several commenters discussed the practice of some larger corporations, which provide sizable support for their employee's credit union, and view membership in the credit union as a company benefit. In other words, if an employee leaves the employ of the company, the credit union also terminates the individual's membership. These commenters believed CUMAA would allow continuation of this practice. The observation was made that a credit union should be able to divest members that have left the employment of the sponsor if that is what the sponsor desires. The Board does not concur with this observation. The Board's view is that Congress established a permanent membership relationship with the credit union, and unless a member is expelled under the provisions of Section 118 in this Act, membership cannot be unilaterally terminated by the credit union. However, the commenters raise a legitimate operational concern. To address this issue, the Board determined that a credit union can limit the services to members in those situations where membership would conflict with sponsor policy and who are no longer in the field of membership. While membership is retained, the delivery of member services can be qualified. It is anticipated that this approach will adequately address the problem.

Grandfather Provision. Section 101 of CUMAA established that membership is grandfathered for persons: (1) in a single common bond credit union; and (2) in groups comprising multiple common bond credit unions as of the time of passage of the Act. It also indicates, that where the groups comprising either the single or multiple common bond credit unions are defined by any particular organization or business entity, the grandfather provisions will ''continue to apply with respect to any successor to the organization or entity.'' One commenter stated that the final rule should state that successors are automatically grandfathered and the statutory mandate is self-executing. The Board does not believe that this provision is self-executing. The regional director must still approve the housekeeping amendment in the charter. Except for documentation from the credit union explaining the new organizational structure, no further documentation will be required. However, for credit unions undergoing a charter conversion, once the charter type is converted, the protection provided by the grandfather provision no longer applies.

III. Chapter 3 of the Chartering Manual

The Board proposed a separate chapter setting forth special policies for low-income credit unions and special chartering policies for underserved areas. The Board's intent was to encourage the formation of new credit unions and the expansion of existing credit unions into underserved and low-income areas.

One commenter supported NCUA's proposals concerning the chartering of low-income credit unions. One commenter requested a new definition of low-income credit unions. The Board believes the current definition of low-income is satisfactory.

CUMAA authorizes credit union service to people of modest means. This is particularly evident with the addition of underserved areas to the field of membership of a federal credit union with the approval of NCUA. The legislation defines an underserved area as a local community, neighborhood, or rural district that is an ''investment area'' as defined in Section 103(16) of the Community Development Banking and Financial Institutions Act of 1994. A credit union adding an underserved area must establish a service facility in the area.

An investment area includes any of the following:

- An area encompassed or located in an Empowerment Zone or Enterprise Community designated under section 1391 or the Internal Revenue Code of 1996 (26 U.S.C. 1391);
- An area where the percentage of the population living in poverty is at least 20 percent and the area has significant unmet needs for loans or equity investments;
- An area in a Metropolitan Area where the median family income is at or below 80 percent of the Metropolitan Area median family income or the national Metropolitan Area median family income, whichever is greater; and the area has significant unmet needs for loans or equity investments;
- An area outside of a Metropolitan Area, where the median family income is at or below 80 percent of the statewide non-Metropolitan Area median family income or the national non-Metropolitan Area median family income, whichever is greater; and the area has significant unmet needs for loans or equity investments;
- An area where the unemployment rate is at least 1.5 times the national average and the area has significant unmet needs for loans or equity investments;
- An area where the percentage of occupied distressed housing (as indicated by lack of complete plumbing and occupancy of more than one person per room) is at least 20 percent and the area has significant unmet needs for loans or equity investments;
- An area located outside of a Metropolitan Area with a county population loss between 1980 and 1990 of at least 10 percent and the area has significant unmet needs for loans or equity investments.

Three commenters completely supported the proposal. One commenter supported NCUA's definition of an underserved area. Three commenters objected to placing a service facility in an underserved area that is added to the credit union's field of membership. The definition of an underserved area and the service facility requirement are statutory and are incorporated into the

final rule. A few commenters requested that an ATM be treated as a service facility. The legislative history of CUMAA clearly indicates that for this provision an ATM is not a service facility.

Two commenters believed NCUA should define service facility in this section to include a credit union's commitment to regular hours on a periodic basis at a local facility, such as a church or community center. The Board agrees with this comment and has incorporated it into the final regulation. One commenter requested that the Board provide an example of an area having ''significant unmet needs for loans or equity investments.'' An example of ''significant unmet needs for loans or equity investments'' is an area where there are few financial institutions or a high ratio of residents in relation to traditional financial institutions.

Although the new legislation specifically authorizes flexible policies regarding multiple common bond credit unions providing service to underserved areas, the Board has determined that previous agency policies allowing similar service to poor and disadvantaged areas should continue. Accordingly, the Board stated that the criteria established for multiple common bond credit unions would also apply to single occupational, single associational, and community credit unions desiring to serve underserved areas. Thirteen commenters approved of NCUA's decision to allow all types of credit union's to serve underserved areas. The proposal has been adopted in the final regulation.

The proposal stated that federal credit unions adding the underserved community must first develop a business plan on how it will serve the community and that NCUA would require periodic reviews on how the credit union is serving the community. Four commenters stated that to encourage credit unions to add underserved areas to their field of membership, NCUA should avoid requiring burdensome reporting requirements to credit unions attempting to service the ''underserved.'' These commenters stated that requiring loan penetration rate and other community statistical information may discourage credit unions from pursuing that important sector of the market. The Board agrees. However, the Board believes it is necessary first to have a business plan to address how financial services will be provided to an underserved areas. Although not required by regulation, the regional director may require periodic service status reports from a credit union about the underserved area to ensure that the needs of the underserved area being met as well as requiring reports before NCUA allows a federal credit union to add an additional underserved area. Although one commenter requested public hearings before adding an underserved area, the Board believes such a requirement will simply add another bureaucratic hurdle and impede service to the underserved.

One commenter questioned why a credit union that adds an underserved area cannot participate in the Community Development Revolving Loan Program (CDRLP). One commenter requested that the final rule state that a credit union that adds an underserved area cannot participate in the CDRLP. One commenter suggested that providing service to an underserved area does not equate to a low-income designation. Only a credit union with a low-income designation may participate in the CDRLP under NCUA Regulations and the FCUA. If a credit union that adds an underserved area qualifies for a low-income designation, it may apply for the designation and be entitled to the benefits of the CDRLP, and the Board encourages eligible credit unions to do so.

Chapter 3 also permitted any multiple common bond credit union to add a low-income association to its field of membership, if all members of the association meet NCUA's definition of low-income. One commenter stated that NCUA should not require that all members of this type of association be low-income. The Board disagrees with this comment. Because a low-income association has limited common bond requirements, changing its membership criteria may invite abuse and vitiate the Board's intent to allow credit unions to serve low-income people.

IV. Chapter 4 of the Chartering Manual

This chapter discusses the requirements and procedures for conversion of a state credit union to a federal credit union and conversion of a federal credit union to a state credit union. The proposed policy for charter conversions was basically the same as current policy. The major change concerned changing the credit union's name on all signs, records, accounts, investments, stationery and other documents. The proposal allowed credit unions to have 180 days from the effective date of the conversion to change its signage and promotional material. The credit union would be able to reissue, with its new name, its outstanding debit cards, ATM cards, credit cards, at the time of renewal. Share drafts with the credit union's name could be used by the member until depleted. This proposal would apply to both types of conversions, state-to-federal and federal-to-state. Under the proposal, if the state credit union is not federally insured, it must change its name and must immediately cease using any credit union documents referencing federal insurance and a federal name, including checks and credit cards.

Four commenters supported all of the provisions in this chapter. One commenter requested a one year time frame to convert signage, promotional materials, etc. One commenter requested that the regional director have the authority to extend the time frame. The Board believes the current time frames are adequate but has provided the regional director with the discretion to extend the time frame for an additional 180 days.

One commenter requested NCUA to exempt converting state credit unions, whose fields of membership do not conform to federal standards, from compliance with NCUA's community charter requirements. The Board believes that this is not permitted under CUMAA. One commenter stated that a state charter converting to a federal charter should be able to continue to serve all of its existing members under the ''once a member, always a member'' policy. The Board agrees with this commenter and a credit union converting to a federal charter can continue to serve members of record after the date of conversion.

One commenter stated that this section should address conversion to a thrift or bank and provide citations to that information. Thrift and bank conversions are addressed in Section 708a of NCUA's Regulations. 12 CFR 708a.

V. Glossary

Three commenters commended NCUA for removing the definition of ''secondary member'' from the glossary. The Board has decided that there is no longer a need for this term and it will not be included in the glossary of the final manual. Nine commenters recommended NCUA also remove the definition of ''primary member'' from the glossary and any other references to it in the final regulation. The Board believes the term ''primary potential member'' is useful when addressing the issue of economic advisability and select group additions and, therefore, is not deleting the reference.

VI. Effective Date

One commenter requested that the manual be made effective six months after publication so that credit unions would have an equitable opportunity to apply for select group expansions, instead of a first-come, first serve approach. The Board is establishing January 1, 1999, as the effective date for this regulation, except for the definitions of ''immediate family member or household'' and ''well-defined local community, neighborhood or rural district,'' which Congress has designated as major rules. The major rules are effective March 5, 1999. The law contemplates an effective date at least 60 days after publication or submission to Congress for major rule provisions. This serves the public interest by providing all parties, including Congress, an opportunity to review and analyze these provisions prior to their effective date. The Board believes that credit unions are continuing to be harmed by the inability to add new groups and any benefit of delaying the effective date is outweighed by the harm to credit unions. Accordingly, the Board for good cause, finds that pursuant to 5 U.S.C. 553(d)(3) the rule shall be effective on January 1, 1999 and without 30 days advance notice of publication.

VII. General Comments on the Format of the Manual

The Board believed the new format of the manual would be more user-friendly by making information easier to locate. Ten commenters stated that the format of the manual is better and easier to read. Three commenters commended NCUA for a well written proposal. Two commenters commended NCUA for the comprehensiveness and clarity of the proposal. A few commenters recommended consolidating parts of the manual. Two commenters believed the format was difficult to use and recommended a revision. A frequent criticism of the previous chartering manual was that it was difficult to locate information quickly about a particular topic as it related to the different types of charters. To eliminate this problem and to ensure that each section was ''self contained,'' the manual segregates each type of charter into sections and addresses all the various issues that may affect that charter type. In so doing, some of the information applicable to all types of charters is repeated in the different sections. Naturally, in repeating similar information, the actual length of the manual is increased.

However, for the general public or the casual user, it makes for a more user-friendly document and facilitates research on the various types of charters.

VIII. Miscellaneous Comments

There were several comments received that did not directly address specific issues in the manual. One commenter questioned whether NCUA will change charters that do not meet the requirements of this proposal. NCUA will not apply this regulation retroactively. CUMAA grandfathered current credit union members and groups. However, NCUA encourages credit unions to examine and update their charters because it will be important for future credit union expansions or mergers. It is always important for a credit union to maintain an accurate and updated charter to ensure that it serve all eligible groups.

Two commenters are concerned that the proposed manual does not include any specific enforcement provisions, examination procedures or language that addresses the remedies for interested parties in the event that a credit union allegedly fails to adhere to the provisions of the manual. The Board believes that the normal examination procedures should be used to ensure compliance with the regulation. If a violation is discovered and cannot be handled at the regional level, appropriate enforcement actions as set forth in NCUA's Regulations and the FCUA will be initiated by the Board.

Two commenters requested that NCUA set forth procedures for chartering a credit union for the primary purpose of making business loans. A new credit union that wishes to be chartered for this purpose will have it included in its charter if the regional director agrees that the credit union can carry out that objective.

As a general observation, IRPS 99–1 applies only to federal credit unions, unless otherwise specified.

IX. Comments From Banks and Bank Trade Organizations

Briefly summarized, the bank commenters argued that NCUA did not interpret CUMAA correctly and that federal credit unions should be subject to taxation like banks. In general, these commenters opposed the definition of occupational common bond, reasonable proximity, service facility, local community, the streamlined approach for community charters with populations of 300,000 or less in a single political jurisdiction, capital adequacy and the definition of low-income credit unions. Some of these commenters supported NCUA's definition of ''immediate family members'' while others opposed it. Most of the commenters believe NCUA's definitions and standards are vague and lack clarity. In general these commenters argued that the proposal defeats the concept of ''meaningful affinity'' found in CUMAA.

The Board has considered all issues raised by these commenters and has previously addressed the major issues in this preamble since other commenters also opposed many of the same provisions. As to the question of taxation, this issue was legislatively addressed in CUMAA at Section 2.(4), which states that ''[c]redit unions, unlike many other participants in the financial services market, are exempt from Federal and most State taxes. . . .''

Finally, many of the commenters stated that the proposed regulation does nothing to encourage the formation of separate credit unions to serve groups of fewer than 3,000 persons. The Board strongly disagrees with this comment. In fact, it is the Board's intent that any group that can meet the economic advisability requirements, should form its own credit union. The Board has simply established criteria that provides guidance based on historical experience relative to those groups that may have the best opportunity to succeed. Every effort will be made to encourage new charters, but operational feasibility and requirements are valid factors and cannot be ignored in the decision making process.

G. Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a regulation may have on a substantial number of small credit unions (primarily those under $1 million in assets). The final rule will not have a significant economic impact on a substantial number of small credit unions and therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has previously determined that several requirements of this final rule constitute collections of information under the Paperwork Reduction Act. The requirements are that federal credit unions: (1) complete a charter application or conversion application; and (2) provide written requests for changes in a credit union's field of membership. These documents are necessary to ensure the safety and soundness of credit unions as well as

ensuring that the legal requirements of the Act have been met. Other aspects of this final rule reduce the paperwork requirements from the current rule.

It is NCUA's view that some aspects of the time it takes a credit union to complete a charter application, charter amendment, or a community conversion or expansion application is not a burden created by this regulation but is the usual and customary practice in the normal operations of a business entity. However, NCUA estimated that it should take a credit union an average of 80 hours to develop a written charter or conversion request. NCUA estimates that it will receive 80 charter or conversion requests in any given year. The annual reporting burden would be 6,400 hours to comply with this requirement. NCUA also estimates that it should take a credit union an average of two hours to provide a written request for changes in a credit union's field of membership. NCUA estimates that it will receive 9,000 of these requests in any given year. The annual reporting burden would be 18,000 hours to comply with this requirement. The total annual burden hours imposed by the proposed rule is 24,400 hours. Two commenters stated that the average of 80 hours to develop a charter conversion package was an insufficient amount of time. The commenters seem to confuse paperwork requirements with oral communications between the credit union and the region. The Board disagrees with the commenters' analysis and believes, on average, this time is sufficient. Furthermore, the Board believes the number of community charter conversions requests and select group expansion request is an accurate estimation.

The reporting requirements in IRPS 99–1 have been submitted to the Office of Management and Budget for approval and the OMB number will be published as soon as it received by NCUA. Under the Paperwork Reduction Act of 1995, no persons are required to respond to a collection of information unless it displays a valid OMB control number. The control number will be displayed in the table at 12 CFR 795.

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. This final rule makes no significant changes with respect to state credit unions and therefore, will not materially affect state interests.

Congressional Review

Congress, by statute, has determined that NCUA's definition of ''immediate family or household'' as well as NCUA's definition of a ''well-defined local community, neighborhood, or rural district,'' shall be treated as a major rule for purposes of chapter 8 of title 5 United States Code. OMB has determined that the remaining provisions of IRPS 99–1 do not constitute a major rule.

List of Subjects in 12 CFR Part 701

Credit, Credit unions, Reporting and recordkeeping requirements.

By the National Credit Union Administration Board on December 17, and December 22, 1998.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Organization and Operations of Federal Credit Unions

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The NCUA is incorporating into its regulations the agency's longstanding interpretation that federal credit unions can permit a nonmember to assume a member's long-term residential real estate loan in conjunction with the nonmember's purchase of the member's principal residence.

EFFECTIVE DATE: January 25, 1999.

ADDRESSES: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428.

FOR FURTHER INFORMATION CONTACT: Michael J. McKenna, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

Since 1977, federal credit unions have had the authority to offer long-term real estate loans to finance a member's principal residence. 12 U.S.C. 1757(A)(i). NCUA's implementing regulation for this authority is set forth at 12 CFR 701.21(g).

In 1985, the NCUA Board issued Interpretive Ruling and Policy Statement 85–3 (IRPS 85–3). 50 FR 51840 (December 20, 1985). IRPS 85–3 stated that, incidental to a federal credit union's authority to make long-term real estate loans to members, a federal credit union may permit assumptions, by either members or nonmembers, under the terms and conditions specified in the loan agreement and consistent with the Federal Credit Union Act and NCUA's Regulations. The NCUA Board also stated that, in the case of a nonmember assumption, there must be no new money lent to the borrower and no extension of the original maturity date specified in the loan agreement with the member.

NCUA has a policy of periodically reviewing its regulations to ''update, clarify and simplify existing regulations and eliminate redundant and unnecessary provisions.'' IRPS 87–2, Developing and Reviewing Government Regulations. As part of its regulatory review program, NCUA reviewed its IRPS to determine their current effectiveness. As a result of that review, the NCUA Board stated that it planned to incorporate IRPS 85–3 into NCUA's Regulations. 62 FR 11773 (March 13, 1997). The Board's goal is to increase regulatory effectiveness by making it easier for credit unions to locate applicable rules regarding real estate lending. Accordingly, at 63 FR 41978 (August 6, 1998), the NCUA Board proposed to add a new paragraph to § 701.21(g) that incorporated IRPS 85–3 so that this provision on nonmember assumption of loans will be in the same place with the other regulatory provisions regarding real estate lending. Although the language is slightly different, the policy set forth in the proposed amendment was, for all practical purposes, identical to the policy set forth in IRPS 85–3.

B. Comments

Five comments were received. Comments were received from one federal credit union, two state leagues, one national credit union trade association, and one bank trade association. Except for the bank trade association, the commenters strongly supported the proposal.

The preamble to the proposed rule, just as IRPS 85–3, stated that a federal credit union cannot grant an assumption of a loan to a nonmember if the underlying intent of the original loan to the member was to grant an assumption by a nonmember immediately or soon after making the original loan. One commenter stated that ''intent'' is an elusive standard and requested that NCUA provide further guidance in the preamble to the final regulation as to how examiners will construct a showing that a loan was originally granted with the intention that it would be assumed by a nonmember. Intent to conduct such a sham transaction is difficult to define. The question of whether there was an improper intent will depend on the facts in a particular case. An example of a suspicious transaction would be one in which a member receives a real estate loan from the credit union and within a short period of time, contracts to sell the property to a nonmember who wants to assume the loan. Although there may be a legitimate reason for this action, NCUA will review the transaction to ensure that it was not done to circumvent the restrictions on providing services to nonmembers.

One commenter requested that NCUA extend the assumption of a loan by a nonmember to automobile loans when the individual who is assuming the loan is either the co-signer or co-owner of the automobile. The NCUA Board does not believe this authority should be extended in this situation since the practice and process of assuming real estate loans is fundamentally different in complexity, maturity, and value than a situation involving automobile loans. In addition, the NCUA Board does not see a great need for extending this assumption authority to automobile loans.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact any proposed regulation may have on a substantial number of small entities (primarily those under $1 million in assets). The NCUA Board has determined and certifies that the final amendment will not have a significant economic impact on a substantial number of small credit unions. Accordingly, the Board has determined that a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final amendment does not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. The final amendment only applies to federal credit unions. NCUA has determined that the final amendment does not constitute a significant regulatory action for the purposes of the Executive Order.

Congressional Review

The Office of Management and Budget has determined that this is not a major rule.

List of Subjects in 12 CFR Part 701

Credit, Credit unions, Insurance, Mortgages, Reporting and recordkeeping requirements, Surety bonds.

By the National Credit Union Administration Board on December 17, 1998.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Organization and Operations of Federal Credit Unions

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The final rule clarifies certain provisions in NCUA's regulation that sets forth the requirements for the purchase, sale and pledge of eligible obligations. Currently, the regulation provides that a federal credit union (FCU) may purchase real estate loans from any source if it is granting real estate loans on an ongoing basis and the purchase will facilitate the packaging of a pool of loans for sale on the secondary market. The final rule clarifies that a pool must include a substantial portion of the FCU's members' loans and must be sold promptly. Further, the final rule explains when the purchase of a member's loan is not the purchase of an eligible obligation, but rather the making of a direct loan.

DATES: The rule is effective January 1, 1999.

FOR FURTHER INFORMATION CONTACT: Mary F. Rupp, Staff Attorney, Office of General Counsel, National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428 or telephone: (703) 518–6553.

SUPPLEMENTARY INFORMATION:

Background

On July 30, 1998, the NCUA Board requested comments on proposed changes to § 701.23 of its regulations. 63 FR 41976 (August 6, 1998). Section 701.23 sets forth the requirements for FCUs' purchase, sale and pledge of eligible obligations.

Section 701.23(b)(1)(iv) allows an FCU to purchase real estate loans from any source if it is granting them on an ongoing basis and the purchase will facilitate the packaging of a pool of loans to be sold on the secondary market. The proposal clarified that a pool of loans, as used in that subsection, must include a substantial portion of the FCU's own loans and must be sold promptly. This clarification is taken from the Accounting Manual. Accounting Manual for Federal Credit Unions, § 6030.4.

Section 701.23(b)(3) sets forth the exceptions to the 5% limit on the purchase of eligible obligations. The proposal adds to the list of exceptions, an indirect lending or leasing arrangement if it is classified as a loan. The conditions for classifying it as a loan are that the FCU must make the final underwriting decision and that the sale or lease contract must be assigned to the FCU very soon after it is signed by the member and the dealer or leasing company.

Summary of Comments

The NCUA Board received ten comments on the proposal: two from credit union trade groups; one from a state league; five from credit unions; one from a bank trade group; and one from a private insurer. Of the six commenters that addressed the proposed changes, five generally supported them.

Section 701.23(b)(1)(iv)

The five commenters that supported the proposed changes to this provision noted that the amendments give sufficient guidance while allowing flexibility. One commenter noted that the amendment has the beneficial effect of preserving credit unions' focus on making loans to members while avoiding the imposition of a barrier if certain timeframes and amounts were required.

The negative commenter was concerned that the language in the proposal requiring ''a substantial portion of its own loans'' would preclude it from having a pool composed substantially of member loans it had purchased from its CUSO. An FCU has the express authority to purchase its member loans from any source without any pooling requirements. 12 U.S.C. 1757(13); 12 CFR 701.23(b)(i). Since the intent of the limitation in § 701.23(b)(iv) is to limit the purchase of nonmember loans, the final rule has been clarified to indicate that a substantial portion of the pool must be composed of ''member loans.''

The Board asked for comment on whether specific numbers should be used instead of the terms ''substantial'' and ''promptly.'' Six of the seven commenters that responded opposed using specific numbers. The reasons cited in opposition were that: setting a fixed ceiling and specific time may make it difficult for an FCU in certain circumstances; placing specific limitations, which remove all flexibility for dealing with unforeseen circumstances, is unnecessary; setting a specific ceiling and using specific dates may make it difficult for large credit unions to assist small credit unions with access to the secondary market; and using specific numbers and dates does not recognize the realities of the secondary marketplace. The Board agrees that it is important for FCUs to have flexibility in this area and so, it will not define ''substantial'' and ''promptly'' with specific numbers.

One commenter, a bank trade group, does not address the proposal, but rather takes exception to § 701.23(b)(1)(iv) since its promulgation in 1979. The bank trade group ''believes that the purchasing of nonmember loans even for the purpose of pooling these loans to be sold on the secondary market is an attempt by federal credit unions to circumvent the restrictions on loans to nonmembers.'' The proposed rule explained in detail the statutory authority for this provision. 63 FR at 41976.

Section 701.23(b)(3).

The two commenters that addressed the issue of clarifying in the rule that indirect lending is considered a loan rather than the purchase of an eligible obligation supported the proposed changes. Three commenters suggested that the preamble to the final rule clarify that credit or electronic scoring by a third party vendor using the credit union's criteria is consistent with the FCU making the final underwriting decision. The NCUA Board agrees with this interpretation which follows General Counsel opinion letters.

Two commenters asked for clarification that assignment of the loan means acceptance of the loan and not necessarily, physical receipt of the loan documentation. The NCUA Board concurs. In today's marketplace, acceptance and payment are often done electronically. However, physical receipt of the loan documents by the credit union should occur within a reasonable time following acceptance of the loan.

The two commenters that responded to the question of whether a specific number of days should be substituted for the language requiring assignment of the contract ''very soon'' after it is signed by the member, opposed specific numbers. The commenters noted that using specific numbers could reduce flexibility and is not necessary. The NCUA Board agrees and will not use specific numbers.

Finally, the NCUA Board asked for comment on whether the types of loans that can be purchased from any source for purposes of creating pools for sale should be expanded to include auto and credit card loans. Five of the six commenters that responded supported the Board pursuing this option for FCUs. Those commenters noted that it would provide credit unions with an important asset and liability management tool for use as an alternative means of creating liquidity.

The one negative commenter did not see the need for a regulation permitting this practice, because there is no major secondary market for auto and credit card loans.

The NCUA Board is aware that there is a growing secondary market for auto and credit card loans and intends to look at whether this is appropriate for FCUs. Currently, the Financial Accounting Standards Board (FASB) is reviewing the accounting standards governing these transactions. Once FASB states its position and there is stability in this area, the NCUA Board will make a decision on whether to expand its regulations to permit FCUs to purchase nonmember auto and credit card loans for sale on the secondary market.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires the NCUA to prepare an analysis to describe any significant economic effect any regulation may have on a substantial number of small credit unions, meaning those under $1 million in assets. The NCUA Board has determined and certifies that the final rule will not have a significant economic impact on a substantial number of small credit unions. The reason for this determination is that it is highly unlikely that small credit unions would be engaged in pooling real estate loans for sale on the secondary market. Accordingly, the NCUA Board has determined that a Regulatory Flexibility Analysis is not required.

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. The final rule will only apply to federal credit unions. Section 741.8(b)(1) specifically exempts state chartered federally insured credit unions from § 701.23(b)(1)(iv). Section 701.23(b)(v) only applies to FCUs.

Paperwork Reduction Act

The final rule does not impose any additional paperwork requirements on FCUs.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedures Act. 5 U.S.C. 551. The Office of Management and Budget has reviewed this rule and determined that, for purposes of the Small Business Regulatory Enforcement Act Fairness Act of 1996, this is not a major rule.

List of Subjects in 12 CFR Part 701

Credit unions; Eligible obligations.

By the National Credit Union Administration Board on December 17, 1998.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Loan Interest Rates

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The current 18 percent per year federal credit union loan rate ceiling is scheduled to revert to 15 percent on March 9, 1999, unless otherwise provided by the NCUA Board (Board). A 15 percent ceiling would restrict certain categories of credit and adversely affect the financial condition of a number of federal credit unions. At the same time, prevailing market rates and economic conditions do not justify a rate higher than the current 18 percent ceiling. Accordingly, the Board hereby continues an 18 percent federal credit union loan rate ceiling for the period from March 9, 1999 through September 8, 2000. Loans and lines of credit balances existing prior to May 18, 1987 may continue to bear their contractual rate of interest, not to exceed 21 percent. The Board is prepared to reconsider the 18 percent ceiling at any time should changes in economic conditions warrant.

EFFECTIVE DATE: March 9, 1999.

ADDRESSES: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia, 22314–3428.

FOR FURTHER INFORMATION CONTACT: Dan Gordon, Senior Investment Officer, Office of Investment Services, at the above address or telephone: (703) 518–6620.

SUPPLEMENTARY INFORMATION:

Background

Public Law 96–221, enacted in 1979, raised the loan interest rate ceiling for federal credit unions from 1 percent per month (12 percent per year) to 15 percent per year. It also authorized the Board to set a higher limit, after consulting with the Congress, the Department of Treasury and other federal financial agencies, for a period not to exceed 18 months, if the Board determined that: (1) money market interest rates have risen over the preceding 6 months; and (2) prevailing interest rate levels threaten the safety and soundness of individual credit unions as evidenced by adverse trends in growth, liquidity, capital, and earnings.

On December 3, 1980, the Board determined that the foregoing conditions had been met. Accordingly, the Board raised the loan ceiling for 9 months to 21 percent in the unstable environment of the first-half of the 1980s. The Board lowered the loan rate ceiling form 21 percent to 18 percent effective May 18, 1987. This action was taken in an environment of falling market interest rates from 1980 to early 1987. The ceiling has remained at 18 percent to the present.

The Board believes that the 18 percent ceiling will permit credit unions to continue to meet their current lending programs, permit flexibility so that credit unions can react to any adverse economic developments, and ensure that any increase in the cost of funds would not affect the safety and soundness of federal credit unions.

The Board would prefer not to set loan interest rate ceilings for federal credit unions. Credit unions are cooperatives that balance loan and share rates consistent with the needs of their members and prevailing market interest rates.

The Board supports free lending markets and the ability of federal credit unions boards of directors to establish loan rates that reflect current market conditions and the interests of their members. Congress has, however, imposed loan rate ceilings since 1934. In 1979, Congress set the ceiling at 15 percent but authorized the Board to set a ceiling in excess of 15 percent, if conditions warrant.

The following analysis justifies a ceiling above 15 percent, but at the same time does not support a ceiling above the current 18 percent. The Board is prepared to reconsider this actions at any time should changes in economic conditions warrant.

Money Market Interest Rates

Interest rates and the expectations about the future level of economic activity have recently been dominated by concerns in worldwide financial markets. The downfall of many Asian economies and the unprecedented recession in Japan required the Federal Reserve, as the central bank most capable of preventing a world-wide economic downturn, to substantially lower interest rates in early October of last year. There are now indications that the actions taken at that time had the intended effect. Several of the Asian economics have recently shown signs of recovery and Japan, recognizing its vulnerability, has undertaken a massive fiscal stimulus package.

The result is that inflation fears in the United States, which only recently were overshadowed by the Asian economic crisis, are reemerging. With the economy still growing in excess of 3.5 percent per annum, and recovery now underway in foreign economies, there are concerns that conditions exist for further inflationary pressures. The recent credit squeeze in financial markets, reflected by tighter bank credit standards and wider credit spreads, has reduced capital expenditures, and thus future productivity gains. Yet the strong productivity gains were a primary factor preventing price increase in the last few years.

The potential scarcity of capital, the prospective improvement in the world economies, and the expectation that oil prices could recover from their now 12-year lows and commodity prices from their 22-year lows will increase inflationary expectations. In addition, strong consumer confidence, a strong housing market and continued expansion in consumer spending will continue to put pressure on the economy. With unemployment remaining in the 4.5 percent range, and the continued strong demand for workers, wage pressures will increase. In addition, as less skilled workers are employed and firms are required to use more scarce resources, the pressures on costs, and thus on prices, will intensify. The result may well be further increases in interest rates.

Reinforcing the expectation of higher rates, the Federal Reserve has strongly suggested it will not lower rates again in the near term. The result has been an expectation in financial markets that interest rates could rise above current levels. Already there have been substantial increases in yields since lows reached in early October. For example, on October 1, 1998, the rate on the 6-month Treasury was 4.36 percent, and on January 5, 1999, it was 4.54 percent. The 5-year Treasury rate was 4.55 percent on January 4, 1999. This was 48 basis points above the rate on October 1, 1998, while the 10-year Treasury rate increased 39 basis points in the same interval. Therefore, although the current rates are below the rates of six months ago, there is every indication that by March 9, 1999, rates will be higher than they were on October 1.

TABLE 1.—TREASURY RATES

Maturity	Yields as of October 1, 1998 (percent)	Yields as of January 4, 1999 (percent)	Change in basis points
3-month	4.22	4.67	25
6-month	4.36	4.54	18
1-year	4.27	4.57	30
2-year	4.15	4.56	41
5-year	4.07	4.55	48
10-year	4.29	4.67	38
30-year	4.88	5.15	27

The fact that long-term rates exceed short-term rates (for example, the 30-year rate is 61 basis points above the 6-month rate) is more evidence that the market expects rates to rise in the months ahead. Investors are unwilling to hold longer term investments unless they are compensated for these potentially higher future rates.

Further declines in the unemployment rate, rising consumer confidence, continued income growth and a strong equity market have led many to be concerned that consumer demand may rise at a faster pace in the months ahead. We need to be aware of these potential inflationary pressures which could result in higher interest rates. Therefore, it is important to maintain the 18 percent ceiling. Lowering the interest rate ceiling at this time could cause an unnecessary burden on credit unions.

Financial Implications for Credit Unions

For at least 873 credit unions, representing 28 percent [1] of the reporting federal credit unions, the most common rate on unsecured loans was above 15 percent. While the bulk of credit union lending is below 15 percent, small credit unions and credit unions that have instituted risk-based lending programs require interest rates above 15 percent to maintain liquidity, capital, earnings, and growth. Loans to members who have not yet established a credit history or have weak credit histories have more credit risk. Credit unions must charge rates to cover the potential of higher than usual losses for such loans. There are undoubtedly more than 873 credit unions charging over 15 percent for unsecured loans to such members. Many credit unions have ''Credit Builder'' or ''Credit Rebuilder'' loans but only report the ''most common'' rate on the Call Report for unsecured loans. Lowering the interest rate ceiling for credit unions would discourage credit unions from making these loans. Credit seekers' options would be reduced and most of the affected members would have no alternative but to turn to other lenders who will charge much higher rates.

Small credit unions would be particularly affected by a lower loan ceiling since they tend to have a higher level of unsecured loans, typically with lower loan balances. Thus, small credit unions making small loans to members with poor or no credit histories are struggling with far higher costs than the typical credit union. Both young people and lower income households have limited access to credit and, absent a credit union, often pay rates of 24 to 30 percent to other lenders. Rates between 15 and 18 percent are attractive to such members.

Table 2 shows the number of credit unions in each asset group where the most common rate is more than 15 percent for unsecured loans.

TABLE 2.—FEDERAL CREDIT UNIONS WITH MOST COMMON UNSECURED LOAN RATES GREATER THAN 15 PERCENT

[June 1998]

Peer group by asset size	Total all FCUs	Number FCUs w/ loan rates >15%
$0–2 mil	1,940	214
$2–10 mil	2,390	334
$10–50 mil	1,735	214
$50 mil+	842	111
Total [1]	6,907	873

[1] Of this total, 4,083 had either a zero balance or did not report rate balances 15 percent and above.

Among the 871 credit unions where the most common rate is more than 15 percent for unsecured loans, 242 have 20 percent or more of their assets (Table 3) in this category. For these credit unions, lowering the rates would damage their liquidity, capital, earnings, and growth.

TABLE 3.—FEDERAL CREDIT UNIONS WITH MOST COMMON UNSECURED LOAN RATES GREATER THAN 15 PERCENT AND MORE THAN 20 PERCENT OF ASSETS IN UNSECURED LOANS

[June 1998]

Peer group by asset size	Avg. percentage of loan rates >15% to assets	Number FCUs meeting both criteria
$0–2 mil	38.31	95
$2–10 mil	28.46	61
$10–50 mil	25.62	22
$50 mil+	23.34	7
Total	32.99	185

In conclusion, the Board has continued the federal credit union loan interest rate ceiling of 18 percent per year for the period from March 9, 1999, through September 9, 2000. Loans and line of credit balances existing on May 16, 1987 may continue to bear interest at their contractual rate, not to exceed 21 percent. Finally, the Board is prepared to reconsider the 18 percent ceiling at any time during the extension period, should changes in economic conditions warrant.

Regulatory Procedures

Administrative Procedure Act

The Board has determined that notice and public comment on this rule are impractical and not in the public interest. 5 U.S.C. 553(b)(3)(B). Due to the need for a planning period prior to the March 9, 1999, expiration date of the current rule, and the threat to the safety and soundness of individual credit unions with insufficient flexibility to determine loan rates, final action of the loan rate ceiling is necessary.

[1] Of the 6,907 FCUs, 4,083 had zero balances in the 15 percent and above category or did not report a balance for the June 1998 reporting period.

Regulatory Flexibility Act

For the same reasons, a regulatory flexibility analysis is not required. 5 U.S.C. 604(a). However, the Board has considered the need for this rule, and the alternatives, as set forth above.

Paperwork Reduction Act

There are no paperwork requirements.

Executive Order 12612

This final rule does not affect state regulation of credit unions. It implements provisions of the Federal Credit Union Act applying only to federal credit unions.

List of Subjects in 12 CFR Part 701

Credit, Credit unions, Loan interest rates.

By the National Credit Union Administration Board on January 28, 1999.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 707

Truth in Savings

AGENCY: National Credit Union Administration (NCUA).

ACTION: Interim final rule with request for comments.

SUMMARY: NCUA is amending part 707 of its regulations to implement certain statutory changes in the Truth in Savings Act (TISA). These amendments: modify the rules governing indoor lobby signs; eliminate subsequent disclosure requirements for automatically renewable term share accounts with terms of one month or less; repeal TISA's civil liability provisions as of September 30, 2001; and permit disclosure of an annual percentage yield (APY) equal to the contract dividend rate for term share accounts with maturities greater than one year that do not compound but require dividend distributions at least annually.

DATES: This rule is effective December 29, 1998. Comments must be received on or before March 29, 1999.

ADDRESSES: Direct comments to Becky Baker, Secretary of the Board. Mail or hand-deliver comments to: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428. You may fax comments to (703) 518–6319. *Please send comments by one method only.*

FOR FURTHER INFORMATION CONTACT: Frank S. Kressman, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

Background

Part 707 of NCUA's regulations implements TISA. 12 CFR part 707. The purpose of part 707 and TISA is to assist members in making meaningful comparisons among share accounts offered by credit unions. Part 707 requires disclosure of fees, dividend rates, APY, and other terms concerning share accounts to members at account opening or whenever a member requests this information. Fees and other information also must be provided on any periodic statement credit unions send to their members. TISA requires NCUA to promulgate regulations substantially similar to those promulgated by the Board of Governors of the Federal Reserve System (Federal Reserve). 12 U.S.C. 4311(b). In doing so, NCUA is to take into account the unique nature of credit unions and the limitations under which they may pay dividends on member accounts.

The Federal Reserve has issued final rules to implement certain statutory changes in TISA. One of these rules: expands an exemption from certain advertising provisions for signs on the interior of a depository institution; eliminates the requirement that depository institutions provide disclosures in advance of maturity for automatically renewable (rollover) accounts with a term of one month or less; and repeals TISA's civil liability provisions, effective September 30, 2001. 63 FR 52105 (September 29, 1998). The Federal Reserve also has promulgated a final rule that permits depository institutions to disclose an APY equal to the contract interest rate for time accounts with maturities greater than one year that do not compound but require interest distributions at least annually. 63 FR 40635 (July 30, 1998). NCUA is issuing final rules that are substantially similar to the above rules issued by the Federal Reserve.

Interim Final Rule

The NCUA Board is issuing these rules as interim final rules because there is a strong public interest in having in place consumer oriented rules that are consistent with those recently promulgated by the Federal Reserve. Additionally, as discussed above, NCUA is required to issue rules substantively similar to those of the Federal Reserve shortly after the Federal Reserve issues its final rules. Accordingly, for good cause, the Board finds that, pursuant to 5 U.S.C. 553(b)(3)(B), notice and public procedures are impracticable, unnecessary, and contrary to the public interest; and, pursuant to 5 U.S.C. 553(d)(3), the rules shall be effective immediately and without 30 days advance notice of publication. Although the rules are being issued as interim final rules and are effective immediately, the NCUA Board encourages interested parties to submit comments.

Section by Section Analysis

Section 707.4 Account Disclosures

A brief statement has been added to the account disclosure requirements of § 707.4(b)(6)(iii) for credit unions stating an APY equal to the contract dividend rate for noncompounding term share accounts that have a maturity greater than one year and that require dividend payouts at least annually. The statement alerts members to the fact that dividends cannot remain in the account. This is intended to assist members in comparison shopping between accounts with annual compounding and accounts that do not compound but require dividend payouts during the account term.

Section 707.5 Subsequent Disclosures

Section 266(a)(3) of TISA requires depository institutions to provide certain disclosures for rollover accounts at least 30 days before maturity. The Federal Reserve has determined that the purposes of TISA would not be served by requiring advance disclosures for rollover accounts with maturities of one month or less, and has interpreted one month to include 30 or 31 days. NCUA takes the same approach in this context, and does not require disclosures to be provided in advance of maturity for these accounts. Credit unions will continue to provide disclosures when these accounts are opened. Accordingly, § 707.5(c) and the corresponding provision in Appendix C-Official Staff Interpretations, which required disclosure, are deleted.

Section 707.8 Advertising

This section requires credit unions that advertise APYs for accounts to disclose other key account features. It requires a brief narrative that parallels the account disclosure statement required by § 707.4(b)(6)(iii). If a credit union states an APY equal to the contract dividend rate in advertising a noncompounding multi-year account that requires dividend payments, the fact that dividend payouts are mandatory and that dividends cannot remain in the account must be stated. This disclosure is intended to assist members in comparison shopping between multi-year accounts that compound annually and multi-year accounts that do not compound but require dividend payouts at least annually.

Section 263(a) of TISA provides that a reference to a specific dividend rate, yield, or rate of earnings in an advertisement triggers a duty to state certain additional information, including the APY. In 1994, Congress amended section 263(c) of the advertising rules to provide that, if a rate is displayed on a sign, including a rate board, designed to be viewed only from the interior of the premises, then the disclosure requirements of section 263 do not apply. A subsequent statutory amendment to section 263(c) expands the exemption for signs on the interior of the premises. Specifically, all signs inside the premises are exempt from certain advertising disclosures, including signs that are intended to be viewed from outside the premises. Accordingly, the reference in § 707.8(e)

to signs that face outside the premises and the corresponding provision in the Appendix C—Official Staff Interpretations are amended. Any sign posted on the outside of the premises remains covered by the advertising provisions unless the sign qualifies for some other exemption, such as the exemption for electronic media.

The Federal Reserve exempts advertisements made through broadcast or electronic media from several of the mandatory advertising disclosures. The Federal Reserve has determined that computer or other advertisements, such as those posted on the Internet, are not exempt under the broadcast or electronic media provision. The rationale for broadcast and electronic media exemptions is that these media have time or space constraints that make it extremely burdensome to provide the required disclosures. Advertisements posted on the Internet generally do not have the same time and space constraints. Such advertisements, therefore, remain subject to the general advertising rules and must comply with the requirements of §§ 707.8(a), (b), (c), and (d).

Section 707.9 Enforcement and Record Retention

Section 271 of TISA, which provides for civil liability for violations of TISA, has been repealed effective September 30, 2001. This section reflects the effective date of the repeal.

Appendix A to Part 707—Annual Percentage Yield Calculation

Paragraph E is added to Appendix A, Part I to clarify how APYs may be determined for noncompounding term share accounts that have a maturity greater than one year and that pay dividends at least annually. Two examples are added, including an example calculating the APY for a stepped-rate account.

Appendix B to Part 707—Model Clauses and Sample Forms

A new model clause is added to describe the effect of dividend payments on earnings.

Appendix C to Part 707—Official Staff Interpretations

Appendix C has been amended in accordance with the amendments made to §§ 707.5 and 707.8 for the reasons discussed above.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact any proposed regulation may have on a substantial number of small entities (primarily those under $1 million in assets). The NCUA has determined and certifies that this interim rule will not have a significant economic impact on a substantial number of small credit unions. Accordingly, the NCUA has determined that a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

This interim rule has no net effect on the reporting requirements in part 707.

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. It states that: ''Federal action limiting the policy-making discretion of the states should be taken only where constitutional authority for the action is clear and certain, and the national activity is necessitated by the presence of a problem of national scope.'' This interim rule will not have a direct effect on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this interim rule does not constitute a significant regulatory action for purposes of the executive order.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedures Act. 5 U.S.C. 551. The Office of Management and Budget has reviewed this rule and has determined that for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996 this is not a major rule.

List of Subjects in 12 CFR Part 707

Advertising, Consumer protection, Credit unions, Reporting and recordkeeping requirements, Truth in savings.

By the National Credit Union Administration Board on December 17, 1998.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 708a

Conversion of Insured Credit Unions to Mutual Savings Banks

AGENCY: National Credit Union Administration (NCUA).

ACTION: Interim final rule with request for comments.

SUMMARY: The NCUA is revising its rules that govern the conversion of insured credit unions to mutual savings banks or savings associations, if the savings associations are in mutual form. These revisions will simplify the charter conversion process and reduce regulatory burden for insured credit unions that choose to convert. NCUA is making these revisions in compliance with recent federal legislation that mandates such revisions.

DATES: This rule is effective November 27, 1998. Comments must be received on or before February 25, 1999.

ADDRESSES: Direct comments to Becky Baker, Secretary of the Board. Mail or hand-deliver comments to: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428. Fax comments to (703) 518–6319. *Please send comments by one method only.*

FOR FURTHER INFORMATION CONTACT: Frank S. Kressman, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

Background

The Credit Union Membership Access Act (the Membership Access Act) was enacted into law on August 7, 1998. Public Law 105–21. Section 202 of the Membership Access Act amends the provisions of the FCU Act concerning conversion of insured credit unions to mutual savings banks or mutual savings associations. Pursuant to the amendments, NCUA is required to promulgate final rules regarding charter conversions within six months that are: (1) consistent with the Membership Access Act; (2) consistent with the charter conversion rules promulgated by other financial regulators; and (3) no more or less restrictive than rules applicable to charter conversions of other financial institutions. Accordingly, NCUA is revising part 708a to implement the provisions of § 202 of the Membership Access Act. NCUA does not interpret the Membership Access Act to preclude state regulatory authorities from imposing more restrictive charter conversion rules on federally insured state-chartered credit unions.

Interim Final Rule

The NCUA Board is issuing this rule as an interim final rule because there is a strong public interest in having rules in place consistent with the requirements of § 202 of the Membership Access Act. If this rule were not effective immediately, there would be no such rule in place to process credit union conversions to mutual savings banks. Accordingly, for good cause, the Board finds that, pursuant to 5 U.S.C. 553(b)(3)(B), notice and public procedures are impracticable, unnecessary, and contrary to the public interest; and, pursuant to 5 U.S.C. 553(d)(3), the rule shall be effective immediately and without 30 days advance notice of publication. Although the rule is being issued as an interim final rule and is effective immediately, the NCUA Board encourages interested parties to submit comments.

Section by Section Analysis

Section 708a.1 Definitions

This section defines a number of terms used throughout part 708a. Although the former part 708a did not contain a section specifically designated for definitions, former § 708a.2(c)(2) defined ''senior management official.'' Revised § 708a.1 expands on that definition to include, at the end of the definition, the phrase ''and any other senior executive officer as defined by the appropriate federal banking agency pursuant to section 32(f) of the Federal Deposit Insurance Act.'' 12 U.S.C. 1831i(f).

Section 708a.2 Authority to Convert

This section restates a portion of the Membership Access Act that provides an insured credit union may convert to a mutual savings bank or a savings association that is in mutual form without the prior approval of NCUA. Although the Membership Access Act eliminates the need for credit unions to obtain NCUA's prior approval, it requires NCUA to administer the membership vote. Also, the vote must be verified by the federal or state agency having jurisdiction over the credit union after the conversion. As provided in § 708a.7 discussed below, if NCUA disapproves of the methods or procedures applicable to the membership vote, it may require that another vote be taken. This section also states that conversions require the approval of the credit union's members and are subject to the laws governing mutual savings banks and savings associations and the other requirements of this part.

Section 708a.3 Board of Directors and Membership Approval

This section provides that the board of directors must approve the proposal to convert by a majority vote and must set a date for a membership vote on the proposal. Membership approval requires an affirmative vote of a majority of those members who vote on the proposal. Former § 708a.5 required a majority vote of the entire membership, not just a majority of those members choosing to vote. The former requirements for NCUA approval of a detailed plan and disclosure statement have been deleted.

Section 708a.4 Voting Procedures

This section sets out the voting and notice requirements for the membership vote on the proposal to convert. It provides that members eligible to vote on the proposal to convert may do so in person at the meeting designated for the vote on the proposal or by written ballot filed by the member. It also provides that the credit union must provide members with notice to the members 90, 60, and 30 calendar days before the date of the vote and a ballot not less than 30 calendar days before the date of the vote. This section describes the basic requirements for the content of the notice, namely, that the notice must adequately state the purpose and subject matter of the proposal and inform members that they may vote either at the meeting or by submission of a written ballot. The notice must set out the date, time, and place for the meeting.

Section 708a.5 Notice to NCUA

This section requires the credit union to provide NCUA with notice of its intent to convert during the 90 calendar day period preceding the date for the membership vote. A credit union may fulfill this notification requirement by providing the NCUA a letter describing the material features of the conversion or a copy of the filing made with another federal or state regulatory agency seeking that agency's approval of the conversion. With the notice to NCUA, a credit union must include a copy of the notice, ballot and all other written materials it has provided or intends to provide to members so that NCUA can fulfill its oversight responsibility regarding the methods and procedures of the membership vote. If it chooses, a credit union may provide notice of intent to convert prior to the 90 calendar day period preceding the

membership vote. If a credit union submits its notice of intent early, the Regional Director will review it and let the credit union know within 30 calendar days if there is a problem with the methods and procedures for the membership vote. This preliminary review is intended to provide time to credit unions, for example, to correct any defects in the notice to members or other problems in connection with the proposed membership vote. In any event, the credit union will still have to comply with the requirement of verifying the membership vote once it is taken and the Regional Director will still have the right to require a new vote if it is determined that the methods and procedures of the membership vote were not conducted properly.

Section 708a.6 Certification of Vote on Conversion Proposal

This section requires the board of directors of the converting credit union to certify to NCUA the results of the membership vote within 10 calendar days after the vote is taken. The board of directors is also required at this time to certify that all notices, ballots and other written materials provided to members were identical to those submitted to NCUA pursuant to § 708a.5 or to provide copies of any new or revised materials and an explanation of the reason for the changes.

Section 708a.7 NCUA Oversight of Methods and Procedures of Membership Vote

The Membership Access Act specifically requires NCUA to participate in the conversion process by overseeing the membership vote concerning the charter conversion. This oversight function centers on reviewing the methods by which the membership vote was taken and the procedures applicable to the membership vote. The Membership Access Act provides that if, upon review of the membership vote, NCUA disapproves of the methods by which the vote was taken or the procedures applicable to the membership vote, then NCUA is authorized to direct a new membership vote be taken on the proposal to convert. NCUA interprets ''methods and procedures'' of the membership vote to include determining that the notice that the credit union sends to its members is accurate and not misleading, that all required notices were timely, and that the membership vote was conducted in a fair and legal manner.

This section provides that, once the Regional Director receives a certification from the converting credit union of the results of the membership vote, the Regional Director will have 10 calendar days to issue a determination regarding the methods and procedures applicable to the membership vote. This section also sets out that the Regional Director's review of the methods and procedures will consider whether the notice was accurate and not misleading, that all required notices were provided and that the membership vote was conducted in a fair and legal manner.

Section 708a.8 Other Regulatory Oversight of Methods and Procedures of Membership Vote

The Membership Access Act requires the federal or state regulatory agency that will have jurisdiction over the financial institution after conversion to verify the membership vote, and has authorized that agency to direct a new membership vote be taken on the proposal to convert if it disapproves of the methods by which the vote was taken or the procedures applicable to the membership vote.

Section 708a.9 Completion of Conversion

This section provides that upon receipt of the approvals discussed in § 708a.7 and § 708a.8, the credit union may complete the conversion transaction. The board of directors of the newly chartered mutual savings bank or mutual savings association is required to certify completion of the conversion transaction to NCUA within 30 calendar days of the effective date of the conversion. Upon receipt of such certification, the NCUA will cancel the credit union's insurance certificate and federal charter, if applicable.

Section 708a.10 Limit on Compensation of Officials

This section provides that directors and senior management officials of a credit union may not receive any economic benefit from the conversion of their credit union other than compensation and benefits paid to them in the ordinary course of business. This section is intended to insure that decisions to convert are based on proper and appropriate business judgment.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact any proposed regulation may have on a substantial number of small entities (primarily those under $1 million in assets). The NCUA has determined and certifies that this interim rule will not have a significant economic impact on a substantial number of small credit unions. Accordingly, the NCUA has determined that a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

The NCUA Board has determined that the notice and disclosure requirements in part 708a constitute a collection of information under the Paperwork Reduction Act. NCUA is submitting a copy of this interim final rule to the Office of Management and Budget (OMB) for its review.

The interim final rule requires an insured credit union that intends to convert to a mutual savings bank or savings association to provide notice and disclosure of its intent to convert to its members and NCUA. It also requires the credit union to provide additional information to NCUA at various points in the conversion process. These notice and disclosure requirements are mandated by the Membership Access Act. They are also necessary to insure safety and soundness in the credit union industry, and to protect the interests of credit union members in the charter conversion context.

The NCUA Board estimates that it will take an average of 15 to 20 hours to comply with the notice and disclosure requirements of part 708a. The NCUA Board also estimates that fewer than 10 insured credit unions will convert per year, so that the total annual collection burden is estimated to be no more than 200 hours.

The Paperwork Reduction Act of 1995 and OMB regulations require that the public be provided an opportunity to comment on information collection requirements, including an agency's estimate of the burden of the collection of information. The NCUA Board invites comment on: (1) whether the collection of information is necessary; (2) the accuracy of NCUA's estimate of the burden of collecting the information; (3) ways to enhance the quality, utility, and clarity of the information to be collected; and (4) ways to minimize the burden of collection of information. Comments should be sent to: OMB Reports Management Branch, New Executive Office Building, Room 10202, Washington, D.C. 20503; Attention: Alex T. Hunt, Desk Officer for NCUA. Please send NCUA a copy of any comments you submit to OMB.

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. The final rule, as does the current rule, applies to all federally insured credit unions, including federally insured state

chartered credit unions. However, since the final rule reduces regulatory burden, NCUA has determined that the final rule does not constitute a ''significant regulatory action'' for purposes of the Executive Order.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedures Act. 5 U.S.C. 551. The Office of Management and Budget is reviewing this rule to determine whether it is major for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 708a

Charter conversions, Credit unions.

By the National Credit Union Administration Board on November 19, 1998.

Becky Baker,

Secretary of the Board.